understandable fashion the cause of the rate change (e.g., inflation, changes in external costs or the addition/deletion of channels). When the change involves the addition or deletion of channels, each channel added or deleted must be separately identified. Notices to subscribers shall inform them of their right to file complaints about changes in cable programming service tier rates and services with this Commission within 45 days of the rate or service change being reflected in their bill, and shall provide the address and phone number of both the local franchising authority and the Cable Services Bureau of this Commission.

(c) Cable systems shall provide written notice to subscribers of subscribers' right to file with the Commission complaints concerning rate changes for cable programming service or associated equipment. This notice shall be provided at the same time as the notice required under paragraph (b) and additionally with the first bill reflecting the rate change. The notice shall state that the subscriber may file the complaint within forty-five days of the date the complainant receives the bill that reflects the rate change, and shall provide the address and phone number of the local franchising authority and the Commission. For rate changes becoming effective before July 15, 1994, operators may provide this notice by any reasonable and feasible means (such as on screen programming or newspaper publication) rather than the written notice otherwise required by this paragraph.

10. A new § 76.986 is added to Subpart N to read as follows:

§ 76.986 "A la carte" offerings.

(a) Collective offerings of unregulated per-channel or per-program ("a la carte") video programming shall not be regulated if:

(1) The price for the combined package does not exceed the sum of the individual charges for each component of service, and

(2) The cable operator continues to provide the component parts of the package to subscribers separately in addition to the collective offering. The second condition will be met only when the per channel offering provides consumers with a realistic service choice. Collective offerings available on April 1, 1993 shall not be regulated if subsequently offered on the same terms and conditions as were in effect on that date.

(b) In reviewing a basic service rate filing, local franchising authorities may make an initial decision addressing whether a collective offering of "a la carte" channels will be treated as an unregulated service or a regulated tier. The franchising authority must make this initial decision within the 30 day period established for review of basic cable rates and equipment costs in § 76.933(a), or within the first 60 days of an extended 120 day period (if the franchise authority has requested an additional 90 days) pursuant to § 76.933(b). The franchising authority shall provide notice of its decision to the cable system and shall provide public notice of its initial decision within seven days pursuant to local procedural rules for public notice. Operators or consumers may make an interlocutory appeal of the initial decision to the Commission within 14 days of the initial decision. Operators shall provide notice to franchise authorities of their decision whether or not to appeal to the Commission within this period. Consumers shall provide notice to franchise authorities of their decision to appeal to the Commission within this period.

(c) A limited initial decision under paragraph (b) of this section shall toll the time periods under § 76.933 within which local authorities must decide local rate cases. The time period shall resume running seven days after the Commission decides the interlocutory appeal, or seven days following the expiration of the period in which an interlocutory appeal pursuant to paragraph (b) of this section may be filed.

(d) A local franchising authority alternatively may decide whether a collective offering of "a la carte" channels will be treated as an unregulated service or a cable programming services tier as part of its final decision setting rates for the basic service tier. That decision may then be appealed to the Commission as provided for under § 76.945.

[FR Doc. 94–8998 Filed 4–14–94; 8:45 am]
BILLING CODE 6712–01–M

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47 CFR Part 76

[MM Docket Nos. 92–266, 92–262; FCC 94–40]

Cable Act of 1992

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: In furtherance of the Commission's implementation of the rate regulation provision of the Cable Consumer Protection and Competition Act of 1992 ("1992 Cable Act," "Cable Act," or "Act"), the Commission adopted a Third Order on Reconsideration clarifying several of the cable rate regulations. The action disposes principally of issues unrelated to the calculation of rates that were raised on reconsideration of the Report and Order in MM Docket No. 92–266 ("Rate Order"), 58 FR 29736 (May 21, 1993), or that were encountered in the Commission's initial implementation of rate regulation. Specifically, the Commission further clarifies the definition of "effective competition" in section 623(l) of the Act; affirms the rules regarding tier buy-through prohibitions; addresses procedural and jurisdictional issues pertaining to the regulatory process, including certification, basic rate decisions, and refund issues; clarifies the rules governing negative option billing practices, evasions, grandfathering of rate agreements, subscriber bill itemization and advertising of rates; considers remaining issues regarding equipment and installation; and clarifies several points with regard to FCC Form 393 (the benchmark calculation form) and FCC Forms 1200 and 1205 (the new calculation forms).

EFFECTIVE DATE: May 15, 1994.

FOR FURTHER INFORMATION CONTACT: Amy Zoslov, (202) 416–0808, or Julie Buchanan, (202) 416–1170, Cable Services Bureau.

SUPPLEMENTARY INFORMATION: This is a synopsis of the Third Order on Reconsideration, adopted February 22, 1994, released March 30, 1994. The complete text of this Order is available for inspection and copying during normal business hours in the FCC Reference Center (room 239), 1919 M Street NW., Washington, DC, and also may be purchased from the Commission's copy contractor, International Transcription Service, at (202) 857–3800, 2100 M Street NW., suite 140, Washington, DC 20037.

Synopsis of the Third Order on Reconsideration

I. Introduction

1. In furtherance of the Commission's implementation of the rate regulation provision of the Cable Consumer Protection and Competition Act of 1992 ("1992 Cable Act," "Cable Act," or "Act"), the Commission adopted a Third Order on Reconsideration clarifying several of the cable rate regulations. The action disposes principally of issues unrelated to the calculation of rates that were raised on reconsideration of the Report and Order in MM Docket No. 92–266 ("Rate Order"), 8 FCC Rcd 5631 (1993); 58 FR 29736 (May 21, 1993), or that were

encountered in the Commission's initial implementation of rate regulation. Specifically, we further clarify the definition of "effective competition" in section 623(l) of the Act, 47 U.S.C. 543(1); affirm our rules regarding tier buy-through prohibitions; address procedural and jurisdictional issues pertaining to the regulatory process, including certification, basic rate decisions, and refund issues; clarify our rules governing negative option billing practices, evasions, grandfathering of rate agreements, subscriber bill itemization and advertising of rates; consider remaining issues regarding equipment and installation; and clarify several points with regard to FCC Form 393 (the benchmark calculation form) and FCC Forms 1200 and 1205 (the new calculation forms).[1]

II. Competition Issues

A. Definitions and Findings of Effective Competition

2. Under the 1992 Cable Act, rate regulation applies only to cable systems that are not subject to "effective competition" as defined in that Act. 47 U.S.C. 543(a)(2). Section 623(l)(1) of the Act further provides that "effective competition" exists if one of three tests is met. Under the second test, effective competition exists if the franchise area is (i) served by at least two unaffiliated multichannel video programming distributors each of which offers comparable video programming to at least 50% of the households in the franchise area; and (ii) the number of households subscribing to programming services offered by multichannel video programming distributors other than the largest multichannel video programming distributor exceeds 15% of the households in the franchise area. 47 U.S.C. 543(l)(1)(B).

3. *Measurement of subscribership.* We previously adopted various rules to implement this second test for effective competition. One of these rules provides that in calculating whether 15% or more of the households in a franchise area subscribe to all but the largest multichannel video programming distributor, we shall consider the subscribership of competing multichannel distributors on a cumulative basis. By this Order, we affirm our previous interpretation that only the subscribers of those multichannel distributors that offer programming to at least 50% of the households in the franchise area shall be included in this cumulative measurement.

4. *Presumption of availability—satellite-delivered services.* The second test for effective competition requires that at least two unaffiliated multichannel distributors each offer comparable programming to at least 50% of the households in a franchise area. We previously concluded that multichannel programming is "offered" if it is both technically available (*i.e.*, it can be delivered to a household with only minimal additional investment by the multichannel distributor) and actually available (*i.e.*, potential subscribers must be aware of its availability from marketing efforts). 47 CFR 76.905(e). The Rate Order stated that multichannel video programming distribution service received from satellites via satellite master antenna television service ("SMATV") or television receive-only earth station ("TVRO") reception is technically available nationwide in all franchise areas that do not, by regulation, restrict the use of home satellite dishes. Rate Order, 8 FCC Rcd at 5659, 60.

5. Because subscription to satellite service is accomplished alternatively through either SMATV or TVRO facilities, we permitted each to be included toward meeting the 15% subscription test, even through SMATV service, taken alone, might not be available to 50% of the households in a franchise area. This Order affirms our belief that satellite service is generally available from one or the other of these complementary sources, and it is reasonable to measure actual acceptance of satellite services in any area by collectively counting both SMATV and TVRO subscribership toward the 15% test.

6. *Program comparability.* The Rate Order also adopted a rule defining when a competing multichannel distributor is offering "comparable programming" under the second test for effective competition. Rate Order, 8 FCC Rcd at 5666, 67. The rule provides that "[i]n order to offer comparable programming * * * a competing multichannel video programming distributor must offer at least 12 channels of video programming, including at least one channel of nonbroadcast service programming." 47 CFR 76.905(g). Since we do not believe that actual channel parity is necessary to provide a competitive alternative, we reject the argument that multichannel distributors must offer roughly the same number of channels in order to meet the test for offering "comparable programming." We also affirm our belief that it is sufficient to use the minimum basic tier as the basis for comparison. Accordingly, we will not change the definition of "comparable programming" adopted in the Rate Order.

7. *Seasonal households and subscribers.* The Rate Order stated that "[e]ach separately billed or billable customer will count as a household subscribing to or being offered video programming services * * *." 47 CFR 76.905(c). In addition, individual units in multiple dwellings buildings are counted as separate households even though they may not be separately billed. *Id.*

8. The term "household" was defined for purposes of the 1990 Census as "all the persons who occupy a housing unit",[2] while "housing units" was defined to include both occupied and vacant units. Thus, "housing units" reflect the total dwelling units in a community, while a count of "households" reflects only occupied units. As used in the Cable Act, we presume that Congress did not intend "households" to have a different meaning than in the 1990 Census. In any event, we believe that the best and most constant indicator of local viewers' choices is represented by the full-time residents of an area. Moreover, it is the full-time residents who are most affected by the determination whether their cable rates are subject to regulation. Consequently, the operator should measure its penetration rate of full-time subscribers as a percentage of full-time households, *i.e.*, by excluding housing units used for seasonal, occasional, or recreational use.[3]

B. Geographically Uniform Rate Structure

9. The 1992 Cable Act requires cable operators to "have a rate structure, for the provision of cable service, that is uniform throughout the geographic area in which cable service is provided over

[1] FCC Form 1200: "Setting Maximum Initial Permitted Rates for Regulated Cable Services Pursuant to Rules Adopted February 22, 1994—First-Time Filers Form"; FCC Form 1205: "Determining Current Equipment and Installation Rates—Equipment Form."

[2] Bureau of the Census, U.S. Dept. of Commerce, 1990 Census of Population, CP–1–1B, Appendix B at B–8.

[3] We will use the U.S. Census Bureau definition for seasonal, recreational, and occasional use:

These are vacant units used or intended for use only in certain seasons or for weekend or other occasional use throughout the year. Seasonal units include those used for summer or winter sports or recreation, such as beach cottages and hunting cabins. Seasonal units may also include quarters for such workers as herders and loggers. Interval ownership units, sometimes called shared ownership or time-sharing condominiums, are also included here.

1990 Census of Housing, General Housing Characteristics, Maryland, at B–12.

its cable system"[4] In the Rate Order, the Commission concluded that this provision was applicable only to regulated services in regulated markets. Rate Order, 8 FCC Rcd at 5896. The Commission then determined that the provision would be enforced on a franchise area by franchise area basis. *Id.* Finally, the Commission found that this provision did not prohibit all differences in rates between customers. Cable operators are not necessarily barred from distinguishing between seasonal and full-time subscribers and from offering promotional rates universally but for a limited time. Also, discounts for senior citizens or economically disadvantaged groups may be set. Additionally, nonpredatory bulk discounts to multiple dwelling units ("MDUs") are permissible if offered on a uniform basis. *Id.* at 5897, 98.

10. The Cable Act is unequivocal in requiring uniformity of rates within a franchise area. The provision is not limited to any particular class or classes of subscribers. In accordance with the statutory mandate, the Rate Order also specifically noted the Commission's concern that bulk discounts not be abused to displace other multichannel video providers from MDUs, which have become important footholds for the establishment of competition to incumbent cable systems. Rate Order, 8 FCC Rcd at 5898. Cable operators are not prevented from meeting competition—as long as the same rate structure is offered to all MDUs in the franchise area. Moreover, cable operators may offer different rates to MDUs of different sizes and may set rates based on the duration of the contract, provided that the operator can demonstrate that its cost savings vary with the size of the building and the duration of the contract, and as long as the same rate is offered to buildings of the same size and contracts of similar duration. Thus, bulk arrangements on a variable basis between MDUs of the same size and contractual duration, though currently allowed by some franchising authorities, are specifically prohibited by the Act.

11. However, we will allow cable operators' existing contracts with MDUs to be grandfathered. We believe that the elimination of existing contracts would be unnecessarily disruptive to those subscribers receiving discounts, as well as to those cable companies offering the discounts. Thus, contracts between cable operators and MDUs entered into on or before April 1, 1993, in which the contract rate is lower than the permitted regulated rate, may remain in effect until their previously agreed-upon expiration date. To the extent the Rate Order may have been interpreted by private parties to supersede existing contracts, which were accordingly rewritten, the terms of such contracts may be reinstituted without violating Commission rules.

12. In addition, we conclude on reconsideration that the uniform rate structure requirements of section 623(d), 47 U.S.C. 543(d), should apply in all franchise areas, irrespective of the presence of "effective competition" as defined in the Act. The specific harms that the rate uniformity provision is intended to prevent—charging different subscribers different rates with no economic justification and unfairly undercutting competitors' prices—could occur in areas with head-to-head competition or low penetration sufficient to meet the Act's definition of "effective competition." This would not only permit the charging of noncompetitive rates to consumers that are unprotected by either rate regulation or competitive pressure on rates, but also stifle the expansion of existing, especially nascent, competition. As the Senate Report states: "This provision is intended to prevent cable operators from having different rate structures in different parts of one cable franchise * * * (and) from dropping the rates in one portion of a franchise area to undercut a competitor temporarily."[5] The statutory language does not provide, and the Senate Report does not suggest, that the rate uniformity provision should be limited to franchise areas where "effective competition" is absent.

III. Tier Buy-Through Prohibition

13. The tier buy-through prohibition of the 1992 Cable Act prohibits cable operators from requiring subscribers to purchase a particular service tier, other than the basic service tier, in order to obtain access to video programming offered on a per-channel or per-program basis. 47 U.S.C. 543(b)(8). An exception is made for cable operators that are not technically capable of complying with this requirement during the next ten years. *Id.* In a previous decision, we adopted an implementing rule that (1) prohibits discrimination between subscribers of the basic service tier and other subscribers with regard to rates charged for video programming offered on a per-channel or per-program basis; (2) forbids any retiering of channels or services intended to frustrate the purpose of the tier buy-through provision; and (3) defines when cable systems are not technically capable of complying with this requirement. Report and Order in MM Docket No. 92–262 ("Tier Buy-Through Order"), 8 FCC Rcd 2274 (1993); 58 FR 19627 (Apr. 15, 1993); 47 CFR 76.921.[6] At that time, we also determined that all cable systems are subject to the tier buy-through prohibition and our implementing rules.[7] *Id.* at note 32.

14. We continue to believe that the tier buy-through provision applies to all cable systems, regardless of whether they are subject to rate regulation. The language of the provision clearly states, without limitation or qualification, that "a cable operator may not require the subscription to any tier other than the basic service tier * * * as a condition of access to video programming offered on a per channel or per program basis." 47 U.S.C. 543(b)(8). Congress could have easily limited this provision to regulated systems by expressly doing so. Accordingly, to provide all cable subscribers with the maximum possible flexibility in paying for those programs they desire, it is necessary to apply the tier buy-through provision to all cable systems.

IV. Procedural and Jurisdictional Issues

A. Certification Process

15. *Franchising authority's decision not to regulate.* In the Rate Order, we analyzed carefully whether we should assert the authority to regulate basic rates when a franchising authority had not sought certification. We emphasized that Congress had vested in local franchising authorities the primary authority to regulate basic rates and that we therefore did not want to override a locality's decision not to regulate rates.

[4] Communications Act of 1934, as amended, ("Communications Act") section 623(d), 47 U.S.C. 543(d).

[5] Senate Committee on Commerce, Science and Transportation, S. Rep. No. 92, 102d Cong., 1st Sess. at 76 (1991). This language also indicates that the term "geographic area" was intended to refer to "franchise area" and not a broader geographic area. See Rate Order, 8 FCC Rcd at 5896, where the Commission considered, and rejected, arguments to define "geographic area" more broadly than a franchise area.

[6] This rule was originally adopted as Section 76.900, but was renumbered and modified in the Rate Order.

[7] After the release of the Tier Buy-Through Order the Commission clarified in the Rate Order that the tier buy-through provision of the 1992 Cable Act "only precludes operators from conditioning access to programming offered on a per-channel or per-program basis on purchasing intermediate tiers." Rate Order, 8 FCC Rcd at 5903, n. 435. Therefore, the provision does not prohibit operators from requiring the purchase of an intermediate tier of cable programming services in order to obtain access to another tier of cable programming services. *Id.* See also 47 CFR 76.921(a). No petitions for reconsideration were filed in the rate proceeding regarding this clarification.

We concluded that we would not assume jurisdiction in cases where a franchising authority does not apply for certification or directly request that the Commission regulate rates. Rate Order, 8 FCC Rcd at 5676.

16. For the time being, we will continue to decline to assert jurisdiction over basic cable service where franchising authorities do not choose to regulate rates themselves. The Act's regulatory scheme vests in franchising authorities the initial decision whether their communities' basic cable service rates should be regulated. Rate Order, 8 FCC Rcd at 5676. In any case where this may work to the detriment of subscribers, they can seek relief from their local authorities through the political processes available to them. However, in the event that basic cable rates remain unregulated in a large number of communities despite evidence that cable operators in those communities are charging unreasonable rates, we will reexamine this issue.

17. *Franchise fee rebuttal showing.* We stated in the Rate Order that we would presume that franchising authorities receiving franchise fees have the resources to regulate rates. A franchising authority seeking to have the Commission exercise jurisdiction over basic rates is thus required to rebut this presumption with evidence showing why the proceeds of the franchise fees it obtains cannot be used to cover the cost of rate regulation. Rate Order, 8 FCC Rcd at 5676. This showing must consist of a detailed explanation of the franchising authority's regulatory program that shows why funds are insufficient to cover basic rate regulation. *Id.* The Commission will assume jurisdiction only if it determines that the franchise fees cannot reasonably be expected to cover the present regulatory program and basic rate regulation. *Id.*

18. We continue to believe that the rebuttal showing requirement is consistent with section 622(i) of the Communications Act. While the Act provides that the Commission cannot directly control the franchising authority's use of the proceeds from the franchise fees, nothing prevents the Commission from basing a judgment on whether to assume regulation of basic tier rates on whether the franchising authority indeed lacks the funds to do so.

19. As to the specific showing required, the franchising authority would simply have to document the funds it raises from franchise fees and any general taxes, estimate the cost of rate regulation, and provide an explanation as to why the funds are insufficient to cover those costs. Some of these factors may include whether the franchise fee collected is less than five percent of the cable operator's gross revenues,[8] and whether costs may be shared among several municipalities by filing joint certifications. As we gain experience reviewing such requests, we will establish standards on a case-by-case basis to determine whether the franchising authority has sufficiently justified its request that the Commission regulate basic cable rates in a particular community.

20. *Voluntary withdrawal of certification.* Although Congress did not specifically provide for the voluntary decertification of franchising authorities, we believe Congress envisioned that franchising authorities would ultimately decide whether rate regulation is appropriate in their communities. Indeed, the fact that franchising authorities have a choice as to whether to seek certification is part of Congress's scheme to vest primary regulatory responsibility in franchising authorities. Accordingly, we will allow certified franchising authorities to notify the Commission that they have decided not to regulate rates, upon their determination that rate regulation would no longer serve the best interests of local cable subscribers.[9] Franchising authorities are specifically prohibited from accepting consideration in exchange for their decision to decertify.

21. *Franchising authority's failure to meet certification requirements.* In the Rate Order, we stated that we would automatically assume jurisdiction over basic cable rates when a franchising authority seeking initial certification does not have the legal authority to regulate rates or does not have rate regulations that are consistent with those of the Commission. In accordance with the Act, we retain jurisdiction in such cases only until the franchising authority has qualified to exercise jurisdiction by submitting a new certification and meeting the required statutory standard. See 47 U.S.C. 543(a)(6); 47 CFR 76.913(a). We indicated, however, that we would allow the franchising authority to cure any defects in its procedural regulations governing rate proceedings before we would assume jurisdiction. Rate Order, 8 FCC Rcd at 5676, 77; 47 CFR 76.910.

22. We believe that our statutory obligations require us to assert jurisdiction over basic rates when a franchising authority's certification effort is denied for failure to adopt regulations that are consistent with the Commission's rate rules. We do not believe Congress intended for a franchising authority to regulate when its regulations will substantially or materially conflict with federal regulations.[10] Nor do we believe Congress intended that there be a regulatory vacuum when a franchising authority has affirmatively sought certification. Once a franchising authority has affirmatively sought certification because it believes basic rates to be unreasonable, and has indicated a willingness to regulate, we will step in to ensure that basic service rates are properly scrutinized until the franchising authority can become certified.

23. *Revocation or certification.* The 1992 Cable Act establishes conditions for the denial or revocation of a franchising authority's certification. As a threshold matter, a franchising authority that seeks to exercise regulatory jurisdiction must meet certain statutory requirements; otherwise the Commission can deny its request for initial certification.[11] If, after a franchising authority has been certified, the Commission finds that the franchising authority has acted inconsistently with the statutory requirements, "appropriate relief" may be granted. However, if the Commission determines, after the franchising authority has had a reasonable opportunity to comment, that the state and local laws and regulations are not

[8] Section 622(b) of the Communications Act allows franchising authorities to collect franchise fees in an amount up to five percent of a cable operator's gross revenues during any 12-month period. 47 U.S.C. 542(b).

[9] The Commission retains the right to review such determinations and seek an explanation from the franchising authority concerning the factual finding underlying its decision to decertify. We will not prohibit a franchising authority from again seeking certification, even after it has decertified. However, if a pattern of repeated certification and decertification develops, we reserve the right to examine the situation to determine whether the franchising authority can justify its determinations as to the propriety of rate regulation in its community.

[10] Indeed, in revocation cases where the Commission determines that a franchising authority's laws and regulations are not in conformance with Commission regulations, the statute instructs the Commission to assume jurisdiction directly. See Communications Act, section 623(a)(5), 47 U.S.C. 543(a)(5).

[11] There are three statutory requirements. First, the franchising authority must adopt and administer rate regulations that are consistent with those of the Commission. Second, the franchising authority must have the legal authority and personnel to implement the necessary regulations. Third, the franchising authority's procedural regulations for rate proceedings must provide interested parties with a reasonable opportunity to comment. See Communications Act, section 623(a)(3) (A)–(C), 47 U.S.C. 543(a)(3) (A)–(C). See also Communications Act, 623(a)(4) (A)–(C), 47 U.S.C. 543(a)(4) (A)–(C) (setting forth that failure to meet three factors is cause for certification disapproval).

in conformance with the regulations prescribed by the Commission to regulate rates, then the Commission must revoke the jurisdiction of the authority. 47 U.S.C. 543(a)(5).

24. We will modify our position on Commission assumption of jurisdiction in revocation cases involving nonconformance with Commission regulations. As a general matter, we will allow a franchising authority to cure any nonconformance with our rules that does not involve a substantial or material regulatory conflict before we will revoke its certification and assume jurisdiction. On the other hand, we believe that the statute compels us to revoke the certification of any franchising authority once we find, after there has been an opportunity to comment, that state and local regulations conflict with our regulations in a substantial and material manner. More specifically, we will revoke the jurisdiction of a franchising authority for nonconformance when the state and local laws involve a substantial and material conflict with our rate regulations.

B. Franchising Authority's Basic Rate Decision

25. *Cost-of-service showings for basic tier rates.* Some local franchising authorities may have resources and personnel sufficient to conduct a review of a rate-setting justification based on an FCC Form 393 (and/or FCC Forms 1200/1205), but not to examine and review a cost-based showing. This concern may have discouraged certification by many local franchising authorities. We believe that the Commission, consistent with the statutorily shared jurisdictional framework for regulation of the basic service tier, should provide assistance to certified local franchising authorities that are unable to conduct cost-based proceedings. Accordingly, on our own motion, we have decided to establish procedures under which the Commission, if requested by the local franchising authority in a petition for special relief under § 76.7 of the Commission's rules, will issue a ruling that makes cost determinations for the basic service tier. The ruling will also set an appropriate cost-based rate and will become binding on the local franchising authority and the cable operator. Specifically, local franchising authorities receiving cost-of-service showings from cable operators seeking to justify either initial rates or rate increases for the basic service tier will be able to obtain such a Commission ruling on their behalf for those submissions pending no more than 30 days before May 15, 1994, or those made on or after that date.

26. Under these procedures, upon receipt of a cost-of-service showing, a local franchising authority will have 30 days to decide whether to seek Commission assistance.[12] If the franchising authority decides to seek Commission assistance, the franchising authority must issue a brief order to that effect, and serve a copy (before the 30-day deadline) on the cable operator submitting the cost showing. In its request for Commission assistance, the local franchising authority must explain its reasons for seeking Commission assistance, such as lack of adequately trained personnel, lack of financial resources, or other exigent circumstances. Upon receipt of the local authority's notice to seek Commission assistance, the cable operator must deliver a copy of the cost showing together with all relevant attachments to the Commission within 15 days.[13]

27. The Commission's determination of cost-based rates for the basic service tier will be governed by Section 76.945 of the Commission's rules and will become binding upon the local franchising authority. The Commission will notify the local franchising authority and the cable operator of its determination and the basic service tier rate, as established by the Commission. The rate will take effect upon implementation by the local franchising authority and the appropriate remedy, if applicable, will be determined by the franchising authority. A cable operator or franchising authority may seek reconsideration by Commission staff, or review by the full Commission, of the staff ruling on the cost-based determination or the rate itself, pursuant to § 1.106 of § 1.115 of the Commission's rules.

28. *Delegation of authority and form of decision.* The Commission clarifies that the authority to make rate decisions and to issue written orders may be delegated to specified governmental agents such as a local cable commission. We find that the 1992 Cable Act does not prohibit franchising authorities, if so authorized by state and/or local law, from delegating their rate-making responsibilities to a local commission or other subordinate entity, even if that entity is not the "franchising authority" entitled to certification under the Act.[14] Any such subordinate entity will be acting as the authorized agent of and at the will and pleasure of the franchising authority, and its actions will be subject to at least the implicit, if not explicit, ratification of the full franchising authorities. In addition, provided that issuance of rate decisions satisfies the Rate Order's public notice requirements,[15] franchising authorities, or the state or local governments, may determine the particular form such rate decisions will take.

29. *Due process concerns.* In the Rate Order, we afforded franchising authorities considerable flexibility regarding the manner in which interested parties may participate in proceedings regarding rates for the basic service tier and accompanying equipment, as long as they provide a reasonable opportunity for consideration of the views of interested parties and act within the prescribed time periods. Rate Order, 8 FCC Rcd at 5716. We also gave franchising authorities the flexibility to decide whether and when to conduct formal or informal hearings, as long as they act on rate cases within the prescribed time periods to provide interested parties with notice and a meaningful opportunity to participate. *Id.*

30. Rather than impose specific procedural requirements on each individual franchising authority, we find it more appropriate at this juncture to remind franchising authorities to examine their current procedural requirements for other local proceedings and determine the best forum for providing due process to cable operators. In any event, a cable operator is not without redress if it determines that the franchising authority has denied the operator its due process rights. Pursuant to Section 76.944 of the Commission's Rules, the cable operator may raise that argument in its appeal to the local courts of the franchising authority's written decision. Rate Order, 8 FCC Rcd at 5729, n. 388; 47 CFR 76.944.

31. *Appeals.* We stated in the Rate Order that cable operators must file

[12] Under the Commission's current rules, if a franchising authority is able to determine that a cable operator's current rates for the basic service tier and accompanying equipment are reasonable under the Commission's rate regulations, the rates will go into effect 30 days after they are submitted. If the franchising authority is unable to determine the reasonableness of the rates within this period, and the operator has submitted a cost-of-service showing, the franchising authority may toll the effective date of the rates in question for an additional 150 days to evaluate the cost showing. See Rate Order, at para. 119; 47 CFR 76.930.

[13] We will classify referrals of cost-of-service cases from local franchising authorities as restricted proceedings for purposes of our *ex parte* rules. Accordingly, *ex parte* presentations are prohibited. See 47 CFR 1.1208 (1992).

[14] Section 602(10) of the Communications Act defines franchising authority as any governmental entity empowered by federal, state, or local law to grant a franchise. 47 U.S.C. 522(10).

[15] Rate Order, 8 FCC Rcd at 5715, 16.

appeals of local rate decisions with the Commission within 30 days of release of the text of the franchising authority's decision. Rate Order, 8 FCC Rcd at 5730, 31; 47 CFR 74.944(b). Oppositions may be filed within 15 days after the appeal is filed, and must be served on the party or parties appealing the rate decision. Replies may be filed seven days after the last day for oppositions and must be served on the parties to the proceeding. 47 CFR 76.944(b).

32. We will amend § 76.944(b) to require any party filing an appeal of a local rate decision to serve a copy of the appeal on the decisionmaking authority. Additionally, where the state is the appropriate decisionmaking authority, the state must forward a copy of the appeal to the appropriate local official(s).[16]

33. *Settlement of rate cases.* We stated in the Rate Order that the regulatory structure established by section 623 of the Communications Act, 47 U.S.C. 543, does not appear to give cable operators the latitude to settle rate cases. Rather, a franchising authority must follow procedures that are consistent with the Commission's rate regulations and make a reasoned decision based on the record. Rate Order, 8 FCC Rcd at 5715, n. 337.

34. For largely the same reasons that we prohibited agreements not to regulate basic rates,[17] we affirm our intention to disallow settlement agreements that are based on factors outside the record of a rate proceeding. permitting such settlements could potentially allow franchising authorities to bargain away subscribers' statutory protection against unreasonable rates. Furthermore, the availability of settlements could increase the number of cost-of-service showings, which would be more suited to negotiated resolutions. Parties in a rate-setting procedure may, of course, stipulate to particular facts and even the final rate level itself, as long as the basis for each such stipulation is clearly articulated, there is some support for each stipulation in the record, and it does not circumvent our rate regulations.

35. *Effective date of rate increases.* In the Rate Order, we noted that unless the franchising authority finds that a proposed increase in basic tier rates is unreasonable, the increase will go into effect 30 days after filing with the franchising authority. If the franchising authority is unable to determine whether the proposed rate increase is reasonable, or if the cable operator has submitted a cost-of-service showing seeking to justify a rate above the presumptively reasonable level, the franchising authority may delay the effective date of the proposed rate for 90 days, or 150 days, respectively. Rate Order, 8 FCC Rcd at 5709.[18]

36. In this Order, we find that where the franchising authority is unable to determine whether a particular portion of a proposed rate increase is reasonable and the questionable portion is clearly severable, a franchising authority may, at its discretion, permit the implementation of portions of a rate increase it finds reasonable while it reviews the reasonableness of other portions. This policy will permit cable operators to recoup as promptly as possible those costs that are deemed acceptable by the franchising authority.

37. *Proprietary information.* In the Rate Order, we stated that franchising authorities will have the right to collect additional information—including proprietary information—to make a rate determination in those cases where cable operators have submitted initial rates or have proposed increases that exceed the Commission's presumptively reasonable level. Rate Order 8 FCC Rcd at 5718–19. We also required franchising authorities to adopt procedures analogous to those contained in Section 0.459 of the Commission's Rules.[19] *Id.*, n. 349. See 47 CFR 76.938.

38. With respect to the franchising authority's right of access to the cable operator's confidential business records, we find that franchising authorities and the parties to a rate proceeding must have access to the information upon which the rate justification is based. Such access is essential to permit the franchising authority to make an informed evaluation, based on complete information, of the reasonableness of the rate in question. Parties participating in the rate proceeding must have access to proprietary information submitted to the franchising authority in order to evaluate the arguments advanced by the cable operator and to help focus the issues. We clarify that franchising authorities are entitled to request information, including proprietary information, that is reasonably necessary to make a rate determination, whether pursuant to a cost-of-service showing or when applying the competitive differential, as clearly stated in the text of the final rule adopted. 47 CFR 76.938. Each request should clearly state the reason the information is needed, and where related to an FCC Form 393 (and/or FCC Form 1200/1205), indicate the question or section of the form to which the request specifically relates.

39. This right of access is limited to that information necessary to support the elements of the particular rate justification at issue, and extends to the franchising authority and, in appropriate circumstances, to the actual parties to a rate proceeding.[20] Section 76.938 governs such access and, to the extent that any state or local laws provide for more limited access to information than the federal rule, they are accordingly preempted.

40. With respect to franchising authorities' obligations regarding public disclosure of proprietary information submitted by cable operators, we find on further reflection that we should not require franchising authorities to adopt procedures that mirror § 0.459, although they may do so in their discretion. We find it neither necessary nor desirable to preempt state and local laws governing access to information. Thus, while as a general matter we believe franchising authorities should consider the interests of cable operators in protecting proprietary information, we now conclude that franchising authorities should proceed in accordance with applicable local and state law rather than mandating the adoption of procedures analogous to our rules. We therefore amend Section 76.938 accordingly.

41. *Forfeitures and fines.* To the extent that franchising authorities may be concerned with the enforcement of their own orders, decisions, and requests for information, we clarify that if a franchising authority has the power under state or local law to impose forfeitures or fines for violations of its rules, orders, or decisions, including filing deadlines and orders to provide information, we see nothing in the Cable Act or our rules which would prevent

[16] We will classify appeals of local rate decisions as restricted proceedings for purposes of our *ex parte* rules. Accordingly, *ex parte* presentations are prohibited. See 47 CFR 1.1208 (1992).

[17] First Order on Reconsideration, Second Report and Order, and Third Notice of Proposed Rulemaking in MM Docket No. 92–266, 9 FCC Rcd 1164 (1993); 58 Fed. Reg. 46718 (Sept. 2, 1993) at para. 72 [hereinafter First Rates Reconsideration].

[18] To toll the effective date of the proposed rate, the franchising authority must issue a brief order, within the initial 30-day period, explaining that it needs additional time to review the proposed rate. *Id.*

[19] Section 0.459 provides that a party submitting information may request confidentiality with respect to specific portions of the material submitted. The party must make a showing, by a preponderance of the evidence, that non-disclosure is consistent with Exemption 4 of the Freedom of Information Act, 5 U.S.C. 552, which authorizes the Commission to withhold from public disclosure confidential commercial or financial information.

[20] Franchising authorities should, in appropriate circumstances, adopt procedures or craft protective agreements to ensure that proprietary information is not disclosed publicly by the parties.

the franchising authority from taking such action.[21] A franchising authority would be free to report to us any apparent violation of our rules, and we could take appropriate enforcement action.[22] In addition, we are modifying our rules to require cable operators to respond to franchising authorities' reasonable requests for information, as well as our own such requests.[23]

42. *Franchising authority discretion.* We also take this opportunity to reiterate our general philosophy regarding rate proceedings before franchising authorities. Congress generally allocated to franchising authorities responsibility for reviewing basic service rates under the Act. While we have set out the general rules for regulation, we have not attempted, nor could we address, every detail of the rate regulation process. Certain latitude has been left to franchising authorities. As we stated in the Rate Order, we will not review decisions of franchising authorities *de novo*, but rather will sustain their decisions as long as there is a reasonable basis for those decisions. Rate Order, 8 FCC Rcd at 5731. This standard of review will apply as well with respect to franchising authority interpretations of any ambiguities in evaluating the responses or information provided on the FCC Form 393 or in a cost-of-service showing.

C. FCC Form 393 (FCC Forms 1200/1205) Issues/Failure to File

43. *Failure to file rate justification.* Under our rules, a cable operator has the burden of proving that its rates for regulated cable services are in compliance with the law.[24] An operator justifies its rates by submitting its rate schedule and by also filing a completed FCC Form 393 (and/or FCC Forms 1200/1205) or a cost-of-service showing. Our rules regarding regulated upper service tiers explicitly provide that if a cable operator fails to file and serve a rate justification as required, we may deem the operator in default and enter an order finding the operator's rates unreasonable and mandating appropriate relief.[25] However, the rules do not explicitly provide parallel remedies where an operator fails to timely justify its rates for the basic service tier.

44. On our own motion, we hereby correct the oversight. An operator that does not attempt to demonstrate the reasonableness of its rates has failed to carry its burden of proof. We are therefore amending our rules to make clear that authorities regulating basic service rates have authority to deem a non-responsive operator in default and enter an order finding the operator's rates unreasonable and mandating appropriate relief. This relief could include, for example, ordering a prospective rate reduction and a refund. Such a refund would be based on the best information available at the time. We note, however, that in the Second Order on Reconsideration, we establish certain adjustments to the timeframes set out in §§ 76.930 and 76.933 due to the transition from existing rules to the rules we establish today.[26] A franchising authority will be permitted to find in default a cable operator that files its rate justification in accordance with the scheme set forth in the Second Order on Reconsideration at paras. 144–149.

45. *Deficient rate justifications; additional information.* In the event a cable operator files a facially incomplete rate justification, *viz.*, fails to complete the FCC Form 393 or fails to include supporting information called for by the form, the franchising authority or the Commission may order the cable operator to file supplemental information. While the francishing authority is waiting to receive this information from the cable operator, the deadlines for the franchising authority to rule on the reasonableness of the proposed rates are tolled.

46. We distinguish an incomplete filing (for example, a form filed without a required explanation) from one which is complete and submitted in good faith, but about which the regulating authority has certain questions or reasonably feels it requires clarifying or substantiating information. However, we will not automatically toll the deadlines for franchising authorities to act in these circumstances, as we do for incomplete filings. If the information sought, however, is of such significance as to delay examination of the rest of the rate justification, or if the operator fails to supply the information promptly, the franchise authority could be justified in delaying its ruling accordingly.

47. In either case, it is obviously necessary for the franchising authority or the Commission to set reasonable deadlines for the submission of supplemental information in order to avoid delaying for consumers the benefits of rate regulation.[27] If the cable operator fails to provide the requested information within the required time or fails to provide complete information in good faith, the franchising authority or the Commission may then hold the cable operator in default and mandate appropriate sanctions as discussed elsewhere in this section, as if the operator failed to submit a response at all. We again emphasize that such authority must be exercised in a reasonable manner.

48. Finally, in order to assist the Commission and franchising authorities in verifying information contained in rate filings, cable operators filing after the effective date of our revised rules must include rate cards and channel line-ups along with their benchmark or cost-of-service filings. If there is any difference between the numbers on these documents and the numbers in the rate filing, the capable operator must attach an explanation. Rate cards and channel line-ups must be included for September 30, 1992, September 1, 1993, and for the rates being reviewed.

49. *Updating rate calculations.* We now turn to the issue that arises for numerous operators that promptly revised their rates in response to our rules, based on rate-setting facts in existence at the time of the revisions. These operators have not been required to justify those rates until recently, however, and several months after the revisions, some of the facts or data on which the rate-setting is based may have changed.[28] For example, tentative inflation adjustments have since become definite, equipment costs may have varied, or broadcast channels may have been added. We recognize that rates adopted in an effort to comply with our rules as quickly as possible may become unreasonable solely as a result of using later data to refresh the calculations. Operators should not be penalized for making good faith attempts to comply with our rules in a timely manner. In addition, if the cable operators are required to revise their rates immediately based on refreshed data, the changes will result in administrative expenses to the operators and confusion for subscribers. In most cases, we expect the resulting rate change would be minimal and would be in effect only until the cable operator seeks a rate

[21] See 47 CFR 76.943. As stated in the regulation, however, a franchising authority may not impose a forfeiture or fine simply because an operator's rates are unreasonable.

[22] See Communications Act, 503, 47 U.S.C. 503; 47 CFR 76.943, 76.963.

[23] See 47 CFR 76.943 (as modified).

[24] 47 CFR 76.937, 76.956(b).

[25] 47 CFR 76.956(e).

[26] Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking in MM Docket 92–266, FCC 94–38, adopted February 22, 1994 [hereinafter Second Order on Reconsideration].

[27] Supporting information that is called for in the FCC Form 393 itself should have been submitted with the form, and could reasonably be demanded within a short period of time.

[28] The same problem could arise any time rates are established at one point in time but subject to justification as of a later date.

change. At the same time, it is important that regulatory authorities are able to verify accurately the reasonableness of a current rate, and to avoid compounding any inaccuracies as subsequent rate increases are introduced, which are a function of the level of initial rates.

50. Accordingly, we will require the following actions when different rates are dictated by data used in initial rate-setting than by data current as of the time an FCC Form 393 (and/or FCC Forms 1200/1205) is actually submitted to the franchising authority or the Commission. When current rates are accurately justified by analysis using the old data (and that data was accurate at the time), cable operators will not be required to change their rates. In these circumstances, however, when such operators make any subsequent changes in their rates, (such as when seeking their annual inflation increase), those changes must be made from rates levels derived from the updated information.[29] When current rates are not justified by analysis using the old data (so that a rate adjustment would be necessary in any event), cable operators will be required to correct their rates pursuant to current data. In these circumstances, the resulting rates must be based on current data.[30]

51. *Computer-generated forms.* Many cable operators have filed their rate justifications on various substitute versions of FCC Form 393, often computer-generated. Indeed, our November 10, 1993 *Public Notice* specifically contemplated such substitutes, provided "the form is *identical* in overall appearance and format to FCC Form 393" (emphasis added). Unfortunately, our initial review of such filings has revealed a wide variety of substitute forms, none of which appears to be "identical in overall appearance and format to FCC Form 393."

52. Given the variations in these forms as filed and the difficulty in verifying their conformance to the official FCC Form 393, we conclude that the burden on franchising authorities and on the Commission of processing such non-standard forms would be substantial. We therefore decide that such substitute forms are unacceptable. All rate filings must be made on an actual FCC Form 393 (and/or FCC Forms 1200/1205), a copy of the actual form, or a copy generated by Commission software.

53. Accordingly, any future rate filing not made on an official FCC Form 393 (and/or FCC Forms 1200/1205), a copy of the form, or a copy generated by Commission software shall be deemed not to have been filed, and appropriate sanctions for failure to file may be imposed. For example, under appropriate circumstances, regulatory authorities may treat non-complying forms as patently defective, thus not requiring an opportunity to cure the defect as would be the case for a filing that is merely incomplete. Obviously, this sanction should not be imposed where an operator has made a good faith effort to comply with our rules. If, however, a cable operator has already made a rate filing on a non-FCC form prior to the effective date of these rules, the franchising authority may order that the form be refiled within 14 days of the effective date of this Order. The cable operator shall then have 14 days to submit its rate filing on an FCC Form 393 (and/or FCC Forms 1200/1205), during which time the deadline for the cable authority to rule on the reasonableness of the rates shall be tolled. Although we considered deeming non-standard forms already filed acceptable, we believe the administrative burden of attempting to implement the rules based on non-complying forms unacceptable. We hereby order all cable operators who have filed benchmark showings with us on a non-FCC form to refile within 14 days of the effective date of this Order. Furthermore, any benchmark showing that comes to the Commission on appeal must be on an official FCC Form 393 (and/or FCC Forms 1200/1205), a copy of the form, or a copy generated by Commission software.

D. Refund Issues

54. *Commission authority to allow franchising authority to order refunds on basic tier rates.* We stated in the April 1993 Rate Order that refunds are available with respect to basic tier service pursuant to our authority under sections 623(b) and 4(i) of the Communications Act, 47 U.S.C. 543(b), 154(i). We determined that the Communications Act's explicit reference to refund authority with respect to upper tier service should not be construed to bar refunds of unreasonable basic tier rates. Rate Order, 8 FCC Rcd at 5725. We noted that section 623(b)(5)(A), 47 U.S.C. 543(b)(5)(A), grants wide discretion to adopt procedures so that franchising authorities can enforce reasonable rates.

55. This Order affirms our belief that section 623(b)(5) grants the Commission wide discretion to craft procedures governing the enforcement of its overall regulatory regime with respect to basic tier rates. The mere fact that section 623(c) provides for refunds in the upper tier context does not persuade us that the Commission's authority under section 4(i), in conjunction with its rulemaking power under section 623(b), is not broad enough to permit the Commission to adopt rules providing for refunds with respect to basic tier rates.

56. *Refund computations.* Another issue which we need to address is that of refund computations for bundled charges. Our rules state that a franchising authority "may order a cable operator to refund to subscribers that portion of previously paid rates determined to be in excess of the permitted tier charge or above the actual cost of equipment * * *."[31] Whereas maximum permitted rates are always determined on an unbundled basis, *i.e.*, separately for tier service and equipment, refund liability may stem from bundled rates.

57. We conclude that the refund liability should be calculated based on the difference between the old bundled rates and the sum of the new unbundled program service charge(s) and the new unbundled equipment charge(s). The intent of the refund mechanism is to place subscribers in the same position they would be had they been subject to "reasonable" rates. To not allow cable operators to factor in equipment charges could result in an operator being required to make a rate reduction that is greater than the maximum reduction required under application of the benchmark approach. This analysis is consistent with our earlier statement that "the cable operator must make prospective billing adjustments to refund overcharges (and offset any undercharges) in a reasonable manner."[32] This analysis also applies to unbundled charges where an operator was charging separately for program services and equipment but the rates did not comply with our rules (because, for example, the equipment rates were higher than actual cost). In this

[29] We take this action on the assumption that any rate differentiation between analysis based on old and current data is quite small, so that the harm to consumers is small compared to the negative effects discussed above. In a particular case where this is not so, the franchising authority can petition for a waiver of our rules to impose an immediate rate reduction.

[30] In any case, the franchising authority retains the discretion to permit retention of an established rate that is close to, but not exactly, the rate justified by our rate formula, with a corresponding reduction taken from the next rate increase, in order to reduce rate churn, if it determines that this best serves the interests of the cable subscribers within its jurisdiction.

[31] 47 CFR 76.942(a).

[32] *Order* in MM Docket No. 92-266, 58 FR 41042, 41044 n.21 (Aug. 2, 1993) (discussing this issue in the context of cable operators not being able to adjust their rates in time when the effective date of regulation was moved from October 1, 1993 to September 1, 1993).

situation, the operator's overall refund liability will be calculated by adding the old charges together and comparing the total with the sum of the new, unbundled program service and equipment charges.

58. *Refunds as affecting franchise fee liability.* Section 622(b) of the Communications Act provides that "[f]or any twelve-month period, the franchise fees paid by a cable operator with respect to any cable system shall not exceed five percent of such cable operator's gross revenues derived in such period from the operation of the cable system." 47 U.S.C. 542(b). We recognize that when a refund is ordered, a cable operator's gross revenue has been reduced, and its franchise fee may have to be reduced proportionately. We amend § 76.942 to provide that, to the extent that a franchise fee is calculated as a percentage of the cable operator's gross revenues and those revenues are reduced on account of refunds, the franchising authority must promptly return to the cable operator the amount that was overpaid as a result of the cable operator's newly-diminished gross revenues.[33]

59. *Calculation of refunds on basic rates.* In the Rate Order and in subsequent orders addressing the effective date of rate regulation,[34] we indicated that cable systems would be subject to potential refund liability for the basic service tier as of the effective date of our rules, which we ultimately determined to be September 1, 1993. See *e.g.*, Rate Order, 8 FCC Rcd at 5725, 26.[35] We will maintain September 1 as the earliest date for refund liability to begin. Any refund liability for this period will be based, of course, on the rate-setting rules and formulas in effect at that time. The new rate-setting rules adopted in the companion Second Order on Reconsideration will be applied prospectively only. The new rules will determine future rates and refund liability only after the effective date of those rules.

60. *Calculation of refunds on cable programming service complaints.* Section 623(c)(1)(C) of the Communications Act, 47 U.S.C. 543(c)(1)(C), requires the Commission to establish procedures (1) to reduce rates for upper tier services that the Commission determines to be unreasonable and (2) to refund overcharges paid by subscribers after the filing of a complaint that the Commission determines to have merit. In the Rate Order, we established that under our refund procedures the cumulative refund due subscribers would be calculated from the date a valid complaint is filed until the date a cable operator implements the reduced rate prospectively in bills to subscribers. Rate Order, 8 FCC Rcd at 5865.[36] We affirm this timeframe for the calculation of refunds and refuse to adopt a time limit on refund liability for unreasonable cable programming service tier rates.

E. Cable Programming Service Complaint Process

61. *Effective date of cable programming service regulation.* We reject suggestions that regulation of upper tier service should commence on the date the Commission's regulations take effect, rather than on the date a complaint is filed. Congress intended regulation of cable programming services to be complaint-driven (see 47 U.S.C. 543(c)(1)(B) and 543(c)(3)). The Commission cannot act on upper tier rates until a complaint is filed. We have decided that complaints that are filed before the effective date of the new rate reductions ordered today in the companion Second Order on Reconsideration will be adjudicated as follows: refunds for the time period in which the old rules were in effect will be based on the old rules, while refunds for the time period in which the new rules are in effect will be based on the new rules.

62. Section 623(c)(3) of the Act directs that complaints must be filed "within a reasonable period of time following a change in rates that is initiated after that effective date, including a change in rates that results from a change in that system's service tiers." 47 U.S.C. 543(c)(3). In the *Rate Order*, we interpreted that provision to require complainants to file such complaints within 45 days from the time a subscriber receives a bill from the cable operator that reflects the rate *increase*. *Rate Order*, 8 FCC Rcd at 5840 (emphasis supplied). We clarify that a subscriber may file a complaint any time there is a rate *change*, including an increase or decrease in rates, or a change in rates that results from a change in a system's service tiers. See 47 U.S.C. 543(c)(3). Such rate changes may involve implicit rate increases (such as deleting channels from a tier without a corresponding lowering of the rate for that tier).[37] As we stated in the *Rate Order*, the triggering mechanism for the filing of the complaint will be a reflection of any rate change on a subscriber's monthly bill. *Id.*[38]

IV. Provisions Applicable to Cable Service Generally

A. Negative Option Billing Practices

63. Section 3(f) of the 1992 Cable Act provides that "a cable operator shall not charge a subscriber for any service or equipment that the subscriber has not affirmatively requested by name."[39] Unlike other subsections of Section 3, this provision does not specifically delineate the jurisdictional role, if any, of state and local governments in addressing negative option billing practices of cable operators.[40] Language in previous decisions in this proceeding has created confusion concerning this issue. Based on our careful examination of the 1992 Cable Act and its legislative history, we conclude that the Commission as well as state and local governments have concurrent

[33] With respect to money that constitutes a franchise fee overcharge resulting from a refund to subscribers pursuant to a rate-setting procedure, and thus owed by a franchising authority to a cable operator, the cable operator may deduct the amount from future franchise fees, rather than have the franchising authority return it in one immediate lump sum payment.

[34] As we have explained before, administrative difficulties necessitated deferral of the original June 21, 1993, effective date for rate regulation to September 1, 1993. See Order in MM Docket No. 92-266, FCC 93-304, 58 FR 33560 (June 18, 1993); Order in MM Docket No. 92-266, FCC 93-372, 58 FR 41042 (August 2, 1993). In all of these orders, we made clear that refund liability would begin as of the effective date of the rules.

[35] Our rules provide that an operator's liability for refunds for basic tier rates is limited to a one-year period, except in cases where an operator fails to comply with a valid rate order issued by a franchising authority or the Commission. In such cases, the operator can be held liable for refunds commencing from the effective date of the order until such time as the operator complies with the order. In all other cases, the refund period shall run as follows: (1) From the date the operator implements a prospective rate reduction back in time to the effective date of the rules, or one year, whichever is shorter; or (2) from the date a franchising authority issues an accounting order, and ending on the date the operator implements a prospective rate reduction ordered by a franchising authority, then back in time from the date of the accounting order to the effective date of the rules, or one year, whichever is sooner. See 47 CFR 76.942 (b) and (c). The effect of these provisions is that refund liability cannot extend back before the effective date of our rates rules.

[36] We further provided that refunds would include interest computed at applicable rates published by the Internal Revenue Service for tax refunds and additional tax payments. Also, interest would accrue from the date a valid complaint is filed until the refund issues. Rate Order, 8 FCC Rcd at 5867. See also 47 CFR 76.961(a)-(d).

[37] See discussion of implicit rate increases in Rate Order, 8 FCC Rcd at 5917.

[38] We amend § 76.953(b), accordingly, to reflect this clarification.

[39] Communications Act, Section 623(f), 47 U.S.C. 543(f).

[40] Compare section 3(f) with section 3(a) (2), (3), providing that local franchising authorities may obtain jurisdiction to regulate basic service tier rates upon certification by the Commission. Communications Act, section 623(a) (2), (3), 47 U.S.C. 543(a) (2), (3).

jurisdiction to regulate negative option billing.

64. On reconsideration, on our own motion, we examine in greater detail whether, and under what circumstances, state and local governments have authority to regulate negative option billing practices of cable operators. We conclude that the 1992 Cable Act permits state and local governments to employ state or local consumer protection laws to regulate negative option billing. State and local government jurisdiction to regulate negative option billing under consumer protection laws is concurrent with the Commission's jurisdiction to regulate negative option billing under the Communications Act. Therefore, based on our close examination of the preemption issue in this order, we hereby substitute this analysis for two statements made in previous orders which could be read to preempt state and local government jurisdiction to regulate negative option billing practices under state and local consumer protection laws.[41]

65. The negative option billing provision appears in section 3 of the 1992 Cable Act, the section of the statute governing rate regulation. Unlike most of the other provisions of Section 3, however, the negative option billing provision is not limited in its application to those cable services and cable operators subject to rate regulation. Rather, than unqualified negative option billing prohibition applies to all cable services offered by all cable operators, regardless of whether the operators are subject to effective competition.[42] Thus, it appears that the negative option billing provision is more in the nature of a consumer protection measure rather than a rate regulation provision *per se*. Section 8(c)(1) of the 1992 Cable Act provides that "[n]othing in this title [Title VI] shall be construed to prohibit any State or any franchising authority from enacting or enforcing any consumer protection law, to the extent not specifically preempted by this title."[43] Therefore, given that section 3(f) appears to be a consumer protection measure, unless "specifically preempted" elsewhere in title VI, section 8(c)(1) preserves the ability of a state or local government to exercise any authority it may have under state or local consumer protection laws to regulate negative option billing.

B. Prevention of Evasions

66. The 1992 Cable Act requires the Commission to establish and periodically review regulations to prevent evasion of the rate regulations, including evasion resulting from retiering. 47 U.S.C. 543(h). The Rate Order defined a prohibited evasion as "any practice or action which avoids the rate regulation provision of the Act or Commission rules contrary to the intent of the Act or its underlying policies." Rate Order, 8 FCC Rcd at 5915. The Commission generally opted for a case-by-case approach and declined to delineate specific actions that might constitute evasion. *Id.*[44]

67. In the Rate Order, we stated our belief that it would be virtually impossible to list potentially evasive practice or to determine that a practice constitutes evasion in the absence of a specific factual context, while expressing our expectations that evasions would be remedied by this Commission and local franchising authorities. *Id.* at 5915, 5916. While we still may be unable to list all prohibited practices at this time, certain patterns of conduct have emerged since the adoption of the rate regulations that we can characterize as creating, under certain circumstances, a possible evasion of the rate regulation rules. For example, moving groups of programming services that were offered in tiered packages to *a la carte* packages may be considered, in certain circumstances, an attempt to avoid the rate regulation of those services that had traditionally been offered to customers as part of the programming package intended for regulation by Congress. Such practices may not, depending on the particular circumstances, provide subscribers with the realistic option to purchase unregulated channels on an individual basis, a requirement set forth in the Rate Order.[45] Generally, as discussed in further detail in the Second Order on Reconsideration at Section II C ("*A la carte*" packages"), collective offerings of otherwise exempt per channel or per program services will not be considered an evasion if (1) the price for the combined package does not exceed the sum of the individual charges for each component of service; and (2) the cable operator continues to provide the component parts of the package separately (which requirement will be met if the *a la carte* offering constitutes a realistic service choice.[46]

68. Collapsing multiple tiers of service into the basic tier of service, which ultimately eliminates the service choice previously available to customers and that raises the price of cable service for all basic tier subscribers may also be considered an evasion by circumventing the rules intended to reduce the cost of cable service and to provide for the buy-through of only desired services.[47] Upon receipt of a complaint on any potential evasion, we will consider, *inter alia*, such circumstances as the timing of the cable operator's actions (*e.g.*, whether it occurred on the eve of regulation or in response to the filing of a complaint), the price to subscribers before and after the actions, a comparison of the level of service received by the subscriber before and after the cable operator's actions, and whether the action resulted in the avoidance of the tier buy-through prohibition. Practices that have the effect of increasing subscriber choice and/or reducing rates generally will not be found evasive of our rules.

69. Numerous other practices that have developed since the advent of rate regulation might also be found, depending on individual circumstances,

[41] One of these statements, in footnote 1095 of the Rate Order, provides that "[w]e do not preclude state and local authorities from adopting rules or taking enforcement action relating to basic services or associated equipment consistent with the implementing rules we adopt and their powers under state law to impose penalties." Rate Order, 8 FCC Rcd at 5905 n.1095. The other statement, in footnote 127 of the First Rates Reconsideration, provides that:

> We similarly affirm that franchising authorities may not regulate tier restructuring in a manner that is inconsistent with the 1992 Cable Act. See Communications Act, Sections 623 (a)(1), (f), 47 U.S.C. 543 (a)(1), (f). In particular, local authorities are precluded from regulating negative option billing to prevent tier restructuring regardless of how the local requirement is characterized. The Commission has ruled that cable operators may engage in revenue-neutral tier restructuring without violating the negative option billing procedure.

Id. at 46 n.127 (internal citation omitted).

[42] The legislative history confirms this conclusion. House Committee on Energy and Commerce, H.R. Conf. Rep. No. 862, 102d Cong., 2d Sess. at 65 (1992) (the prohibition covers, *inter alia*, "individually-priced programs or channels" that are not subject to rate regulation under the 1992 Cable Act); 138 Cong. Rec. S567–68 (daily ed. Jan. 29, 1992) (remarks of Sen. Gorton, sponsor of the provision).

[43] Communications Act, Section 632(c)(1), 47 U.S.C. 552(c)(1).

[44] In the Rate Order, the Commission did cite three practices that, if established by the evidence, would constitute evasions. This list, however, was not meant to be an exhaustive delineation of rate regulation evasions, but rather was to serve as the foundation for developing policies in this area. Rate Order, 8 FCC Rcd at 5917.

[45] *Id.* at 5837, n.808.

[46] See also interpretive guidelines on whether collective offerings of *a la carte* channels should be accorded regulated or nonregulated treatment, as discussed in the Second Order on Reconsideration at Section II C. As noted therein, packages of *a la carte* channels offered prior to April 1, 1993 will be accorded nonregulated treatment.

[47] The "price to subscribers" and "comparison of the level of service" for purposes of determining whether an operator's collective offering of *a la carte* channels should be accorded regulated or nonregulated treatment or will be considered an evasion will be evaluated within the context of the factors set forth in the Second Order on Reconsideration.

to constitute evasions of the rules or to violate the rules themselves. For instance, operators cannot now charge for services previously provided without extra charge (*e.g.*, routine service calls, program guides) unless the value of that service, as now reflected in the new charges, was removed from the base rate number when calculating the reduction in rates necessary to establish reasonable rates. Also, a single channel provided to the customer that may consist of two or more programming services can be counted only as one channel of service provided for rate-setting purposes. Charging customers to downgrade from service packages that were added without their explicit consent, even where those service packages include previously subscribed services, may be a violation or an evasion of the negative option prohibition. In addition, the delivery of new packages (ironically intended to represent subscriber choice) without an affirmative assent from the subscriber may violate negative option requirements and result in a refund to the customer. Adding previously unneeded equipment and charging for that equipment in order to provide customers with the same services they received previously may also be an evasion of our rules. Operators must realize that these and similar practices, and other practices which directly violate or evade our rules will not be permitted, and that sanctions will be imposed in appropriate circumstances.

C. Grandfathering of Rate Agreements

70. The 1992 Cable Act's grandfather clause allows a franchising authority with a franchise agreement executed before July 1, 1990, that was regulating basic cable rates at that time, to continue such regulation for the remaining term of that agreement without following the Commission's substantive rate standards. 47 U.S.C. 543(j). The Rate Order correctly limited this provision to its explicit terms. Rate Order, 8 FCC Rcd at 5926.

D. Subscriber Bill Itemization

71. *Special taxes.* The 1992 Cable Act allows a cable operator to separately identify certain charges on its bill. *i.e.* the amounts of the bill (1) assessed as a franchise fee (as well as the identity of the franchising authority); (2) assessed to satisfy any requirements the franchise agreement imposes on the operator for costs related to public, educational, or governmental (PEG) channels; and (3) attributable to charges a governmental authority imposes on the transaction between the operator and the subscriber. 47 U.S.C. 542(c). The Rate Order limited the itemization provision to its express terms and found that itemized costs must be direct and verifiable,[48] as well as a reasonable allocation of overhead, and for PEG costs, the sum of the per-channel costs for the number of channels used to meet franchise requirements. Rate Order, 8 FCC Rcd at 5967, 68. The Rate Order also made clear that section 622(c) does not require operators to undertake itemization of any costs. *Id.* at 5967. In the Rate Order, the Commission specifically determined that taxes imposed on rights-of-way and also applicable to other utilities would not be part of a franchise fee and thus could not be itemized, and specifically excluded from itemization California's possessory interest tax. *Id.* at 5968, n. 1399.

72. We have already found ourselves unable to conclude that the California possessory interest tax is, in every instance, a tax on the transaction between the operator and subscriber. See First Rates Reconsideration, *supra* note 17, at para. 106. We found that with varying applications of the tax in different jurisdictions within California, different treatments under our rules would pertain from case to case. Where the assessment of the possessory interest tax is directly related to subscriber revenues, such as where the tax is based on a value of intangible assets formula affectively calculated from the operator's income for the provision of cable service, then it could be accorded external cost treatment, and it similarly would be eligible for itemization on subscriber bills. *Id.* at para. 107. Otherwise it is eligible for neither treatment. As we stated in that earlier decision, we are prepared to allow itemization of utility user taxes in California, or any other jurisdiction, if additional evidence regarding their application in specific instances demonstrates such treatment is warranted under this analytical framework.

73. *Advertising of rates.* The Rate Order prohibited cable operators from advertising prices for cable service that do not include the amount of franchise fees. Rate Order, 8 FCC Rcd at 5972, n. 1415. We remain concerned that consumers could be misled as to the cost of cable services by advertisements which do not include complete rates, and cable operators generally will be required to advertise rates that include all costs and fees. However, in those cases where a system covers multiple franchise areas that have differing franchise fees or other franchise costs, different channel line-ups, or have slightly different rate structures, an operator should be permitted some flexibility for efficient advertising that will reasonably advise potential subscribers of the true cost of service. In such circumstances, an operator can advertise a range of fees, or a "fee plus," rate that indicates the core rate plus the range of possible additions, based on the particular location of the subscriber.[49] An operator need not indicate the total rate for each individual area in such circumstances.

74. *Itemization of "Franchise Related" costs.* We clarify that the costs required under a franchise agreement for "support of institutional networks, free wiring of public buildings, provision of special municipal video services and voice and data transmissions" are properly classified as PEG-related and are therefore itemizable under section 622(c)(2). Rate Order, 8 FCC Rcd at 5967–69.

V. Equipment and Installation

A. Promotions

75. In the Rate Order we stated that operators would be afforded substantial discretion to offer promotions, including a below cost offering for some equipment and installations. Rate Order, 8 FCC Rcd at 5819, 20. Additionally, we stated that certain limits would apply. *Id.* at 5820–21. Consistent with these statements, Section 76.923(j) of our rules allows promotions but limits the recovery, stating: "Operators may not recover the cost of promotional offerings by increasing program service rates above the maximum monthly charge per subscriber prescribed by these rules." Although the rules do not state how in the normal course of setting rates such recovery is to be effected, they do allow that "as part of a general cost-of-service showing, an operator may include the cost of promotions in its general system overhead costs."[50]

76. We believe that our rules do not prevent the recovery of costs of equipment and installations provided to customers free or at reduced rates for the purpose of promoting services. Further, we expect that the benchmark rates already reflect an element of promotional costs because, prior to the

[48] The House Report states that a cable operator shall itemize "only [the] direct and verifiable costs" associated with the categories of costs the Act specifies and should "not include in itemized costs indirect costs." House Committee on Energy and Commerce, H.R. Rep. No. 628, 102d Cong., 2d Sess. at 86 (1992).

[49] For instance, an advertisement might declare that basic service is $14.00 per month plus a franchise fee of 28¢ to 70¢, depending on location, or that it is $14.28 to $14.70, depending on location.

[50] 47 CFR 76.923(j).

inception of benchmark rates, it was fairly routine in the cable industry to periodically run promotional offerings to entice customers to purchase cable services. Considering this, we believe that we have adequately provided for the recovery of promotional offerings when setting the benchmark rates themselves. To the extent that this does not apply to any operator, that operator may attain recovery, if justified, by making a cost-of-service showing. In such case, the costs of promotional offerings may be included, pursuant to § 76.924, in general system overheads. We will, however, continue to monitor this issue. If we find that over time there is evidence that such costs have not been adequately provided for under our existing approach, we will consider any appropriate revisions to our rules or policies at that time.

B. Seasonal Property Related Charges

77. Some operators experience seasonally high maintenance costs associated with the need to turn service on and off at the beginning and end of the season for resort properties. Others provide special maintenance at a special fee that allows seasonal subscribers to avoid the inconvenience of having to disconnect and reconnect at the end and beginning of each season. We do not find that provision should be made for such operators to allow the rates for service to remain higher than average by allowing the cost for the seasonal turn-on and turn-off to remain in the rates for programming service. First of all, these operators are allowed to include the revenues from seasonal orders in their benchmark calculations of rates per channel in effect at September 30, 1992 and on the initial date of regulation.[51] They eliminate the associated costs in determining the maximum allowable rates because these costs are recoverable from separate rates for equipment. If seasonal operators wish to provide special charges for seasonal connect/disconnect services or for off-season maintenance, they may calculate rates for such on Line 7e of Form 393, Part III (or Line 7.e Step B, Equipment and Installation Worksheet, FCC Form 1205), in accordance with our rules.

C. Sale of Home Wiring

78. The Commission requires that upon termination of service, home wiring must be offered for sale to subscribers. Such wiring is to be priced at the replacement cost of the installed material on a per foot basis.[52] There is currently no required schedule for calculation of the charges allowable for home wiring sold to cable customers. It has not been demonstrated that a significantly unique and complicated situation prevails for pricing of home wiring and consequently that a special form is needed. We thus will not impose the additional burden of a special schedule for home wiring. Nevertheless, we clarify that adequate documentation should be maintained to demonstrate compliance with Commission pricing requirements for home wiring as well as for other equipment sold and for installations.

D. Time Lag

79. In the Rate Order, the Commission directed operators to establish an equipment basket for accumulation of equipment and installation costs but did not establish the time periods for measuring equipment basket costs. The Form 393 and related instructions, however, generally require inclusion of historical costs rather than historically-based projected costs. In other words, the actual costs of the year ending are used for the development of rates for the upcoming year instead of projected costs. However, we believe that our methodology, as modified on reconsideration, does not prevent timely recovery of unusually high costs for equipment and installation. We have provided a methodology that eliminates the cost of equipment from service rate calculation because there is a provision to calculate separate rates for installations and equipment. Further, we have clarified in the First Rates Reconsideration that adjustments for unusual changes in operations are permitted, subject to regulatory approval, by using a representative month for developing equipment rates. First Rates Reconsideration, *supra* note 17, at para. 67. Since we believe that this provision will allow operators to recover the full cost of equipment, we will not allow cable operators to use *pro forma* expense figures averaged over the life of the franchise.

VI. Ordering Clauses

80. Accordingly, *It is Ordered* That part 76 of the Commission's rules, 47 U.S.C. part 76, *Is Amended*, as indicated below, May 15, 1994.

81. *It is Further Ordered* That the Petitions for Reconsideration *Are Granted* in part, *Denied* in part, as indicated above, and to the extent that Petitions raise issues concerning leased access rates, they will be disposed of in future orders.

List of Subjects in 47 CFR Part 76

Cable television.

Federal Communications Commission.

William F. Caton,

Acting Secretary.

Rule Changes

Part 76 of title 47 of the Code of Federal Regulations is amended as follows:

PART 76—CABLE TELEVISION SERVICE

1. The authority citation for part 76 continues to read as follows:

Authority: Secs. 2, 3, 4, 301, 303, 307, 308, 309, 48 Stat., as amended, 1064, 1065, 1066, 1081, 1082, 1083, 1084, 1085, 1101; 47 U.S.C. secs. 152, 153, 154, 301, 303, 307, 308, 309, 532, 533, 535, 542, 543, 552 as amended, 106 Stat. 1460.

2. Section 76.905 is amended by revising paragraph (c) to read as follows:

§ 76.905 Standards for identification of cable systems subject to effective competition.

* * * * *

(c) For purposes of paragraphs (b)(1) through (b)(3) of this section, each separately billed or billable customer will count as a household subscribing to or being offered video programming services, with the exception of multiple dwelling buildings billed as a single customer. Individual units of multiple dwelling buildings will count as separate households. The term "households" shall not include those dwellings that are used solely for seasonal, occasional, or recreational use.

* * * * *

3. Section 76.914(a)(1) is revised to read as follows:

§ 76.914 Revocation of certification.

(a) A franchising authority's certification shall be revoked if:

(1) After the franchising authority has been given a reasonable opportunity to comment and cure any minor nonconformance, it is determined that state and local laws and regulations are in substantial and material conflict with the Commission's regulations governing cable rates.

* * * * *

4. Section 76.917 is added to subpart N to read as follows:

§ 76.917 Notification of certification withdrawal.

A franchising authority that has been certified to regulate rates may, at any time, notify the Commission that it no

[51] 47 CFR 76.922.

[52] See Report and Order in MM Docket No. 92-260, 8 FCC Rcd 1435, 1437 (1993); 58 Fed. Reg. 11970 (Mar. 2, 1993), petitions for recon. pending. See also Communications Act, Section 624(i); 47 U.S.C. 544(i).

longer intends to regulate basic cable rates. Such notification shall include the franchising authority's determination that rate regulation no longer serves the interests of cable subscribers served by the cable system within the franchising authority's jurisdiction, and that it has received no consideration for its withdrawal of certification. Such notification shall be served on the cable operator. The Commission retains the right to review such determinations and to request the factual finding of the franchising authority underlying its decision to withdraw certification. The franchising authority's withdrawal becomes effective upon notification to the Commission.

5. Section 76.922(b) is amended by adding paragraph (b)(9) to read as follows:

§ 76.922 Rates for the basic service tier and cable programming services tiers.

* * * * *

(b) * * *

(9) *Updating Data Calculations.*

(i) For purposes of this section, if:

(A) A cable operator, prior to becoming subject to regulation, revised its rates to comply with the Commission's rules; and

(B) The data on which the cable operator relied was current and accurate at the time of revision, and the rate is accurate and justified by the prior data; and

(C) Through no fault of the cable operator, the rates that resulted from using such data differ from the rates that would result from using data current and accurate at the time the cable operator's system becomes subject to regulation;

then the cable operator is not required to change its rates to reflect the data current at the time it becomes subject to regulation.

(ii) Notwithstanding the above, any subsequent changes in a cable operator's rates must be made from rate levels derived from data [that was current as of the date of the rate change].

(iii) For purposes of this subsection, if the rates charged by a cable operator are not justified by an analysis based on the data available at the time it initially adjusted its rates, the cable operator must adjust its rates in accordance with the most accurate data available at the time of the analysis.

* * * * *

6. Section 76.923 is amended by adding paragraph (m) to read as follows:

§ 76.923 Rates for equipment and installation used to receive the basic service tier.

* * * * *

(m) Cable operators shall maintain adequate documentation to demonstrate that charges for the sale and lease of equipment and for installations have been developed in accordance with the rules set forth in this section.

7. Section 76.930 is revised to read as follows:

§ 76.930 Initiation of review of basic cable service and equipment rates.

A cable operator shall file its schedule of rates for the basic service tier and associated equipment with a franchising authority within 30 days of receiving written notification from the franchising authority that the franchising authority has been certified by the Commission to regulate rates for the basic service tier. Basic service and equipment rate schedule filings for existing rates or proposed rate increases (including increases in the baseline channel change that results from reductions in the number of channels in a tier) must use the appropriate official FCC form, a copy thereof, or a copy generated by FCC software. Failure to file on the official FCC form, a copy thereof, or a copy generated by FCC software, may result in the imposition of sanctions specified in § 76.937(d). A cable operator shall include rate cards and channel line-ups with its filing and include an explanation of any discrepancy in the figures provided in these documents and its rate filing.

8. Section 76.933 is amended by adding paragraph (d) to read as follows:

§ 76.933 Franchising authority review of basic cable rates and equipment costs.

* * * * *

(d) A franchising authority may request, pursuant to a petition for special relief under § 76.7, that the Commission examine a cable operator's cost-of-service showing, submitted to the franchising authority as justification of basic tier rates, within 30 days of receipt of a cost-of-service showing. In its petition, the franchising authority shall document its reasons for seeking Commission assistance. The franchising authority shall issue an order stating that it is seeking Commission assistance and serve a copy before the 30-day deadline on the cable operator submitting the cost showing. The cable operator shall deliver a copy of the cost showing, together with all relevant attachments, to the Commission within 15 days of receipt of the local authority's notice to seek Commission assistance. The Commission shall notify the local franchising authority and the cable operator of its ruling and of the basic tier rate, as established by the Commission. The rate shall take effect upon implementation by the franchising authority of such ruling and refund liability shall be governed thereon. The Commission's ruling shall be binding on the franchising authority and the cable operator. A cable operator or franchising authority may seek reconsideration of the ruling pursuant to § 1.106(a)(1) of this chapter or review by the Commission pursuant to § 1.115(a) of this chapter.

9. Section 76.937 is amended by adding paragraphs (d) and (e) to read as follows:

§ 76.937 Burden of proof.

* * * * *

(d) A franchising authority or the Commission may find a cable operator that does not attempt to demonstrate the reasonableness of its rates in default and, using the best information available, enter an order finding the cable operator's rates unreasonable and mandating appropriate relief, as specified in §§ 76.940, 76.941, and 76.942.

(e) A franchising authority or the Commission may order a cable operator that has filed a facially incomplete form to file supplemental information, and the franchising authority's deadline to rule on the reasonableness of the proposed rates will be tolled pending the receipt of such information. A franchising authority may set reasonable deadlines for the filing of such information, and may find the cable operator in default and mandate appropriate relief, pursuant to paragraph (d) of this section, for the cable operator's failure to comply with the deadline or otherwise provide complete information in good faith.

10. Section 76.938 is revised to read as follows:

§ 76.938 Proprietary information.

A franchising authority may require the production of proprietary information to make a rate determination in those cases where cable operators have submitted initial rates, or have proposed rate increases, pursuant to an FCC Form 393 (and/or FCC Forms 1200/1205) filing or a cost-of-service showing. The franchising authority shall state a justification for each item of information requested and, where related to an FCC Form 393 (and/or FCC Forms 1200/1205) filing, indicate the question or section of the form to which the request specifically relates. Upon request to the franchising authority, the parties to a rate proceeding shall have access to such information, subject to the franchising authority's procedures governing non-disclosure by the parties. Public access

to such proprietary information shall be governed by applicable state or local law.

11. Section 76.939 is added to subpart N to read as follows:

§ 76.939 Truthful written statements and responses to requests of franchising authority.

Cable operators shall comply with franchising authorities' and the Commission's requests for information, orders, and decisions. No cable operator shall, in any information submitted to a franchising authority or the Commission in making a rate determination pursuant to an FCC Form 393 (and/or FCC Forms 1200/1205) filing or a cost-of-service showing, make any misrepresentation or willful material omission bearing on any matter within the franchising authority's or the Commission's jurisdiction.

12. Section 76.942 is amended by revising paragraphs (a), (c)(2), and adding paragraphs (c)(3) and (f) to read as follows:

§ 76.942 Refunds.

(a) A franchising authority (or the Commission, pursuant to § 76.945) may order a cable operator to refund to subscribers that portion of previously paid rates determined to be in excess of the permitted tier charge or above the actual cost of equipment, unless the operator has submitted a cost-of-service showing which justifies the rate charged as reasonable. An operator's liability for refunds shall be based on the difference between the old bundled rates and the sum of the new unbundled program service charge(s) and the new unbundled equipment charge(s). Where an operator was charging separately for program services and equipment but the rates were not in compliance with the Commission's rules, the operator's refund liability shall be based on the difference between the sum of the old charges and the sum of the new, unbundled program service and equipment charges. Before ordering a cable operator to refund previously paid rates to subscribers, a franchising authority (or the Commission) must give the operator notice and opportunity to comment.

* * * * *

(c) * * *

(2) From the date a franchising authority issues an accounting order pursuant to § 76.933(c), to the date a prospective rate reduction is issued, then back in time from the date of the accounting order to the effective date of the rules; however, the total refund period shall not exceed one year from the date of the accounting order.

(3) Refund liability shall be calculated on the reasonableness of the rates as determined by the rules in effect during the period under review by the franchising authority or the Commission.

* * * * *

(f) At the time a franchising authority (or the Commission, pursuant to paragraph (a) of this section) orders a cable operator to pay refunds to subscribers, the franchising authority must return to the cable operator an amount equal to that portion of the franchise fee that was paid on the total amount of the refund to subscribers. The franchising authority must promptly return the franchise fee overcharge either in an immediate lump sum payment, or the cable operator may deduct it from the cable system's future franchise fee payments.

13. Section 76.943 is amended by revising paragraph (b) and adding paragraph (c) to read as follows:

§ 76.943 Fines.

* * * * *

(b) If a cable operator willfully fails to comply with the terms of any franchising authority's order, decision, or request for information, as required by § 76.939, the Commission may, in addition to other remedies, impose a forfeiture pursuant to section 503(b) of the Communications Act of 1934, as amended, 47 U.S.C. 503(b).

(c) A cable operator shall not be subject to forfeiture because its rate for basic service or equipment is determined to be unreasonable.

14. Section 76.944 is amended by revising paragraph (b) to read as follows:

§ 76.944 Commission review of franchising authority decisions on rates for the basic service tier and associated equipment.

* * * * *

(b) Any participant at the franchising authority level in a ratemaking proceeding may file an appeal of the franchising authority's decision with the Commission within 30 days of release of the text of the franchising authority's decision as computed under § 1.4(b) of this chapter. Appeals shall be served on the franchising authority or other authority that issued the rate decision. Where the state is the appropriate decisionmaking authority, the state shall forward a copy of the appeal to the appropriate local official(s). Oppositions may be filed within 15 days after the appeals is filed, and must be served on the party(ies) appealing the rate decision. Replies may be filed 7 days after the last day for oppositions and shall be served on the parties to the proceeding.

15. Section 76.945(b) is revised to read as follows:

§ 76.945 Procedures for Commission review of basic service rates.

* * * * *

(b) Basic service and equipment rate schedule filings for existing rates or proposed rate increases (including increases in the baseline channel change that results from reductions in the number of channels in a tier) must use the official FCC form, a copy thereof, or a copy generated by FCC software. Failure to file on the official FCC form or a copy may result in the imposition of sanctions specified in § 76.937(d). Cable operators seeking to justify the reasonableness of existing or proposed rates above the permitted tier rate must submit a cost-of-service showing sufficient to support a finding that the rates are reasonable.

* * * * *

16. Section 76.946 is added to subpart N to read as follows:

§ 76.946 Advertising of rates.

Cable operators that advertise rates for basic service and cable programming service tiers shall be required to advertise rates that include all costs and fees. Cable systems that cover multiple franchise areas having differing franchise fees or other franchise costs, different channel line-ups, or different rate structures may advertise a complete range of fees without specific identification of the rate for each individual area. In such circumstances, the operator may advertise a "fee plus" rate that indicates the core rate plus the range of possible additions, depending on the particular location of the subscriber.

17. Section 76.953(b) is revised to read as follows:

§ 76.953 Limitation on filing a complaint.

* * * * *

(b) *Complaint regarding a rate change.* Except as provided in paragraph (a) of this section, a complaint alleging an unreasonable rate for cable programming service or associated equipment may be filed against a cable operator only in the event of a rate change, including an increase or decrease in rates, or a change in rates that results from a change in a system's service tiers. A rate change may involve an implicit rate increase (such as deleting channels from a tier without a corresponding lowering of the rate for that tier). A complaint regarding a rate change for cable programming service or associated equipment may be

filed against a cable operator only in the event of a rate change. A complaint regarding a rate change for cable programming service or associated equipment must be filed with the Commission within 45 days from the date the complainant receives a bill from the cable operator that reflects the rate change.

* * * * *

18. Section 76.956(a) is revised to read as follows:

§ 76.956 Cable operator response.

(a) Unless the Commission notifies a cable operator to the contrary, the cable operator must file with the Commission a response to the complaint filed on the applicable form, within 30 days of the date of service of the complaint. The response shall indicate when service occurred. Service by mail is complete upon mailing. See § 1.47(f) of this chapter. The response shall include the information required by the appropriate FCC form, including rate cards, channel line-ups, and an explanation of any discrepancy in the figures provided in these documents and the rate filing. The cable operator must serve its response on the complainant (and, if the complainant is a subscriber, the relevant franchising authority) via first class mail.

* * * * *

19. Section 76.961 is amended by revising paragraph (b) and adding paragraph (e) to read as follows:

§ 76.961 Refunds.

* * * * *

(b) The cumulative refund due subscribers shall be calculated from the date a valid complaint is filed until the date a cable operator implements a prospective rate reduction as ordered by the Commission pursuant to § 76.960. The Commission shall calculate refund liability according to the rules in effect for determining the reasonableness of the rates for the period of time covered by the complaint.

* * * * *

(e) At the time the Commission orders a cable operator to pay refunds to subscribers, the franchising authority must return to the cable operator an amount equal to that portion of the franchise fee that was paid on the total amount of the refund to subscribers. The franchising authority may return the franchise fee overcharge either in an immediate lump sum payment, or the cable operator may deduct it from the cable system's future franchise fee payments.

20. Section 76.984 is revised to read as follows:

§ 76.984 Geographically uniform rate structure.

(a) The rates charged by cable operators for basic service, cable programming service, and associated equipment and installation shall be provided pursuant to a rate structure that is uniform throughout each franchise area in which cable service is provided.

(b) This section does not prohibit the establishment by cable operators of reasonable categories of service and customers with separate rates and terms and conditions of service, within a franchise area. Cable operators may offer different rates to multiple dwelling units of different sizes and may set rates based on the duration of the contract, provided that the operator can demonstrate that its costs savings vary with the size of the building and the duration of the contract, and as long as the same rate is offered to buildings of the same size with contracts of similar duration.

(c) Contracts between cable operators and multiple dwelling units entered into on or before April 1, 1993 may remain in effect until their previously agreed-upon expiration date.

[FR Doc. 94–9050 Filed 4–14–94; 8:45 am]
BILLING CODE 6712–01–M

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47 CFR Part 76

[MM Docket No. 93–215, CS Docket No. 94–28; FCC 94–39]

Cable Television Act of 1992

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: The Commission has adopted a Report and Order and a Further Notice of Proposed Rulemaking establishing rules to implement the cost of service alternative to the primary benchmark/price cap approach to setting regulated cable service rates. The Further Notice of Proposed Rulemaking (FNPRM) segment may be found elsewhere in this **Federal Register**. The Report and Order sets forth regulatory requirements to govern cost-of-service showings for cable operators who elect to justify rates above levels determined under benchmark/price cap requirements. The Report and Order, summarized here, adopts a regulatory model based on the cost-of-service formulation that permits cable operators to recover reasonable operating expenses and a fair return on investment, while protecting consumers from unreasonably high rates. Although the Report and Order adopts requirements designed to be consistent with the Commission's telephone ratebase/rate of return formula, the requirements are simpler and easier to administer than the telephone model and can accommodate individual case review. The Report and Order establishes (1) procedural and filing requirements for cost-of-service showings; (2) rules for determining the cable operator's ratebase; (3) rules for determining the appropriate level of recoverable expenses; (4) an interim overall return of 11.25% on ratebase; (5) accounting and cost allocation requirements; (6) accounting and cost allocation requirements for external cost treatment; (7) requirements for affiliated transactions; (8) streamlined filing requirements for small systems; (9) streamlined filing requirements for network upgrades; (10) procedures for emergency rate review based on a showing of special circumstances; and (11) an experimental Upgrade Incentive Plan.

EFFECTIVE DATE: May 15, 1994.

FOR FURTHER INFORMATION CONTACT: JoAnn Lucanik (202) 416–1163; Paul D'Ari (202) 416–1166; John Adams (202) 416–1165.

SUPPLEMENTARY INFORMATION: The text of this document is available for inspection and copying during normal business hours in the FCC Reference Center (Room 239), 1919 M Street, NW., Washington, DC 20554, and may be purchased from the Commission's copy contractor, International Transcription Service, (202) 857–3800, 2100 M Street, NW., Washington, DC 20037.

Synopsis of the Report and Order

The Commission began its implementation of the 1992 Cable Act with an initial Notice of Proposed Rulemaking (Notice of Proposed Rulemaking in CC Docket No. 93–215, FCC 93–353, 58 FR 40762, released July 30, 1993), and established initial rules to implement the Cable Act of 1992 in the Rate Order.[1] The Commission adopted a benchmark and price cap approach to serve as the primary regulatory mechanism for setting initial

[1] Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, Rate Regulation, Notice of Proposed Rulemaking in MM Docket No. 92–266, 58 FR 48, released January 4, 1993; (NPRM); Report and Order and Further Notice of Proposed Rulemaking, 58 FR 29736, released May 21, 1993 (Rate Order); Second Further Notice of Proposed Rulemaking in MM Docket No. 92–266, 58 FR 41042, released August 18, 1993 (Second Notice); First Reconsideration Order, Second Report and Order, and Third Further Notice of Proposed Rulemaking in MM Docket No. 92–266, 58 FR 4678, released Sept. 29, 1993 (First Rates Reconsideration); Third Report and Order in MM Docket No. 92–266, 58 FR 60141, released November 15, 1993.

regulated rates and for governing rates on a going forward basis. The Commission also concluded in the Rate Order that the benchmark/price cap framework might not produce fully compensatory rates in all cases, and accordingly decided to permit cable systems to establish rates based on costs pursuant to individual cost-of-service showings. The cost-of-service approach was to serve as a backup to the benchmark/price cap mechanism which a cable operator could invoke if it believed that the maximum rate under the benchmark/price cap formula would not enable the operator to recover costs that it reasonably incurred in the provision of regulated cable services.

The Rate Order concluded that the use of the benchmark/price cap approach as the primary regulatory mechanism, and the use of a cost-of-service safety valve as a supplemental mechanism, for regulating cable services is fully consistent with the applicable statutory requirements. However, the record in MM Docket 92–266 did not provide sufficient information to allow for development of detailed cost-of-service rules for the cable industry. Accordingly, the Commission indicated that general cost of service principles would apply for cost-of-service showings for the time being, and the present proceeding was initiated by issuing a Notice of Proposed Rulemaking that invited comment on the adoption of cost-of-service goals and rules, and on the role that a cost-based approach to ratemaking should play in our regulation of cable service rates.[2]

This Report and Order establishes rules implementing a cost of service alternative to our primary benchmark and price cap approach to setting regulated cable service rates.[3] In this Report and Order the following regulatory requirements to govern cost-of-service showings are adopted:

The regulatory requirements adopted in the Report and Order are on an interim basis, pending completion of cost studies of the cable industry as described elsewhere in the FNPRM. The interim rules, which apply only in cases where the cable operator elects to rely on a cost-of-service showing rather than on benchmark/price cap requirements, will apply to rates charged or to be charged after the effective date of the cost rules; general cost of service principles will govern rates in effect prior to the effective date of these rules. Thus, to the extent that a franchising authority's examination of basic rates relates to both periods, it would apply the appropriate rules to each period. The Commission will take a similar approach to resolve cable programming complaints that cover both periods. Subsequent cable programming service complaint proceedings or basic tier proceedings relating to rates while the interim rules remain effective will be determined in accordance with the interim rules if the cable operator elects to justify rates as cost-based. If the permanent rules differ from the interim rules, the permanent rules will apply to proceedings relating to rates after their effective date.

Cost of Service Rates Effective

The Report and Order requires that the rate established in a cost-of-service proceeding is the permitted rate, even if it is lower than the rate that would have been determined under the benchmark/price cap approach. Once a rate is established through a cost-of-service proceeding, the rate will be governed by the price cap mechanism.

(1) Procedural and Filing Requirements

Two year interval and election by cable operator only. The Report and Order requires that after setting initial regulated rates under either the benchmark or cost-of-service approach, absent a special showing, operators may not file a cost-of-service showing to justify a new rate for two years. This two-year period will be measured from the effective date of the rates set in a local or Commission decision. The Report and Order finds that a period of two years is a reasonable frequency limitation and will adequately reflect changes in both cost and revenue. A two-year period will also allow for the development of regulatory stability, and the reduction of regulatory burdens. This approach will lessen the administrative burdens of duplicative cost-of-service showings, while furnishing operators a reasonable opportunity to recoup the costs of providing regulated cable services. Although the rules adopted in the Report and Order do not foreclose a cable operator's presenting new cost-of-service data to justify a rate that exceeds the capped rate after a two-year period, multiple cost-of-service showings should be rare, since future adjustments to rates are provided for under the price cap mechanism. The Commission may find it reasonable, following a cost-of-service showing, to set rates that include a scheduled reduction or other adjustment; or may establish rates that are not expected to change, other than under the price cap, pending subsequent cost-of-service showings.

The Report and Order does not allow for local franchising authorities to initiate cost-of-service proceedings or general data collections. Any benefits that might be derived from such a provision would be outweighed by the cost, and could conflict with the statutory requirement to minimize the administrative burdens of rate regulation. Moreover, the primary benchmark/price cap approach to setting rates will assure that rates for regulated cable service are reasonable. Accordingly, the election to choose to set rates pursuant to a cost-of-service showing remains with the cable operator, the Report and Order does not provide for local authorities to initiate cost of service regulation.

Presumptive standards. While the rules adopted in the Report and Order are of general applicability, the rules establish presumptive standards that operators may seek to overcome in individual proceedings. Thus, in certain circumstances, as described further in the Report and Order, operators can present evidence seeking to justify higher rates than would otherwise be permitted under the cost rules. This provision assures that application of the cost rules will not adversely impact the cable industry, and achieves the goal of assuring that cable operators can recover reasonable costs of providing service in high cost areas. Thus, the cost of service alternative provides a safeguard for the industry from possible adverse effects in individual cases of the primary, benchmark/price cap approach and from any adverse effects resulting from general applicability of the cost rules.

Cost of service form. The Report and Order adopts the use of a uniform cost of service form. Use of a form will lessen administrative burdens for industry and regulators by providing uniformity in presentation and review of cost information. The cost of service form will provide a clear standard for the cost support required from operators, and permit easy comparison with previously filed information. The Report and Order adopts a general cost of service form and a simplified cost of service form for small systems; operators seeking to justify rates based on cost of service are required to use one of these two forms. Form 1220 is the general cost of service form in hard copy; Form 1225 is the simplified

[2] Notice of Proposed Rulemaking in MM Docket No. 93–215, FCC 93–353, 58 FR 40762, released July 30, 1993 (Notice).

[3] In a separate decision, the Commission is adopting significant modifications to the benchmark and price cap approach to setting regulated cable service rates. Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket 92–266, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, FCC 94–38 (Benchmark Order).

version of the cost of service form, for small systems, in hard copy. The forms are being released as separate documents. Operators may attach additional worksheets to explain form entries or unusual circumstances. In addition, cable operators must submit with their cost of service form, FCC Forms 1200, 1210, 1211, and 1215 to show the rate that will be permitted under the benchmark/price cap approach.

For purposes of evaluating proposed rates in pending cost-of-service proceedings for the period that commences after the effective date of these new cost rules, the Report and Order requires that all cable operators with pending cost-of-service proceedings for any regulated tier file the cost of service forms that are being adopted with this Report and Order by July 14, 1994.

(2) Rules for Determining Ratebase

The Report and Order adopts the used and useful and prudent investment standards to govern amounts that may be included in the ratebase. The used and useful and prudent investment standards allow into the ratebase portions of plant that directly benefit the ratepayer, and exclude any imprudent, fraudulent, or extravagant outlays.

Valuation of ratebase at original cost. The Commission considered various approaches to determining the value of plant included in the ratebase, including: Market value, original cost, replacement cost, reproduction cost, a combination of these approaches, and other approaches that were proposed by commenters. The Report and Order notes that under applicable judicial precedent, regulators have wide discretion to select a methodology for purposes of valuating ratebase, provided that the end result is reasonable, and the approach selected should be the one that best implements the goals for cost-based rates of cable service.

The Report and Order concludes that an original cost approach is most likely to produce fair and reliable valuations of plant in service, and allows the best opportunity for balancing operators' reasonable recovery of costs with consumers' payment of rates that reflect only costs reasonably incurred in providing regulated service. The Report and Order goes into considerable detail addressing the other methods proposed by commenters for valuation of the ratebase, and finds that none of the other valuation approaches provides the same reliability and fairness as the original cost valuation approach.

For purposes of the cable cost-of-service rules, the Report and Order defines original cost as the actual money cost (or the money value of any consideration other than money) of property at the time it was first used to provide cable service. Costs for both constructed and purchased systems will be subject to scrutiny by the appropriate regulatory authority to determine whether the investment was prudent and the plant is used and useful.[4]

The Report and Order notes that original cost is the normal, now traditional method used for public utility valuation, and is the method this Commission has long used for telephone companies. By relying on actual expenditures rather than speculative or contentious valuation methods, original cost is far more likely to achieve the desired result: Reasonable rates for customers, a fair opportunity for a reasonable return for operators, and reduce administrative burdens. The practical benefits of original cost valuation in general are that it is less administratively burdensome on all involved, and well understood.

Thus, unlike the other valuation approaches, original cost does not require estimates of current values that may be difficult or expensive to determine, and that are in any event likely to be largely matters of opinion. Unlike market-based valuation methods, it does not present the problem of circularity, where the valuation method chosen itself affects the value that the market is likely to place on the system. It is also not constantly changing as the economy, technology, and customer needs change. Original cost valuation is also recognized and defined, and used for financial accounting purposes, as part of Generally Accepted Accounting Principles (GAAP). Indeed, it has been the Commission's policy in recent years to bring its regulatory accounting into conformance with GAAP as far as possible.[5] Use of original cost for cable systems will help implement this policy and minimize regulatory accounting burdens.

The Report and Order took note of the numerous comments arguing that original cost is often simply unascertainable, and found that there is validity in this argument in some cases for purchased systems. The Report and Order acknowledges that use of an estimated original cost when actual original cost is not available is provided for under telephone regulation, 47 CFR 32.2000(b)(2)(ii). Because this approach creates the need for individual scrutiny not only of the estimated original cost but also of underlying "particulars," this is not a preferred alternative to original cost for cable services regulation. However, the Report and Order determines that in the event that an operator does not possess adequate records of original cost, the operator will be permitted to estimate original cost. The operator will be required to show the basis for the estimate with supporting documentation. In addition, the Report and Order permits valuation of tangible plant in service at the book value recorded by the operator at the time of acquisition, if the operator can demonstrate that book value approximates original cost. All cost showings for acquired systems must include the book value of tangible plant in service as recorded at the time of acquisition, as required on Forms 1220 and 1225.

The Report and Order recognizes that original cost valuation, like any valuation methodology, has theoretical limitations—in this case, that it is a backward-looking approach to costs. However, these limitations do not prevent it from being a practical, workable foundation for establishing the value of tangible plant in service. To the extent that use of original cost for computing the ratebase affects the risks that investors may assign to cable systems, the Report and Order takes account of such risks in determining a reasonable rate of return that will allow the system to operate successfully and attract the necessary capital. Thus, in setting the rate of return, the Commission has adopted a rate toward the high end of the zone of reasonable returns, as a cautious approach to assure continued incentives for future investment.

Accumulated start-up loses. The Report and Order concludes that some accumulated start-up losses, to the extent that they reflect operating losses in the early years of the system, should be included in the ratebase. These losses could be considered to meet the used and useful standard in that it is

[4] The regulator may examine whether the construction costs were reasonable, whether plant is operating at a reasonable level of capacity, and whether costs are properly apportioned between regulated and nonregulated activities. In this respect the Commission requires operators subject to regulation under section 623 of the Communications Act, 47 U.S.C. 543, to keep, maintain and protect records subject to regulations adopted in this Report and Order for a period of not less than 5 years. The Commission has authority to take this action under sections 4(i) and 623 of the Communications Act, 47 U.S.C. 4(i) and 543.

[5] See, *e.g.*, Revision of Uniform System of Accounts, Classes A, B, and C Telephone Companies, CC Docket No. 78–196, Report and Order, 51 FR 43498, Dec. 2, 1986. Continuing this Commission's reliance on GAAP, the Commission directs that GAAP shall generally apply in our regulation of cable rates, unless specifically noted otherwise.

frequently necessary for businesses during a start-up phase to sustain a period of losses prior to profitability. As such, the losses benefit customers because it is necessary for the operator to incur them in order to bring future service to subscribers. There is a concern, however, that current customers not be burdened with excessive or unreasonable costs from previous periods of operation; that cable operators' recovery of these costs not be unlimited in time, especially after the losses have been recouped; and that subscribers not pay for losses incurred in expectation of recovery of future supra-competitive profits.

The Report and Order relies on Financial Accounting Statements Board Standard No. 51 ("FASB 51") which suggests that a two-year period is a reasonable and representative start-up time for cable systems. Based on the record, the Report and Order determines that this period would permit recovery of losses necessary for start-up of a cable system, and that a subscriber base is likely to be well established by the end of the second year of operation. Therefore, an allowance is made for recovery in the ratebase of accumulated start-up losses that are equal to the lesser of the first two years of operating costs or accumulated losses incurred until the system reaches the end of its prematurity stage as defined by FASB 51. The Commission believes that losses incurred during this period are most directly linked to the creation of the system that is currently providing services to subscribers.

Cable operators are, of course, free to make a showing that demonstrates the appropriateness of a practical adjustment to this rule in light of their particular circumstances. Operators are also free to present evidence to rebut disallowance of other accumulated losses. In challenging this or any presumptive disallowance, the operator must present detailed evidence demonstrating that the cost has produced a tangible benefit for subscribers that would not have existed but for the cost; and that the relevant plant is used and useful in the provision of regulated cable service, and represents a prudent investment. The operator may present evidence that allowance is necessary for compensatory rates. In making its determination, the regulatory authority should take into account the effect that allowance of these will have on the operator's rates in comparison to rates that would have developed in a competitive environment, and whether allowance of these costs will produce reasonable rates.

The Report and Order finds that these accumulated start-up losses may be included in the ratebase, and the operator may earn on them the reasonable rate of return as defined below. However, these accumulated losses must be amortized over a reasonable period. The Report and Order finds that presumptively this amortization period should not be longer than fifteen years. The Report and Order requires the cable operator to submit detailed evidence of the effect the amortization period has on rates in comparison to competitive rates of similar systems. The Report and Order allows the regulatory authority, after careful scrutiny, to revisit the amortization period if it will produce unreasonable rates. The Report and Order holds that, unless otherwise provided by this Commission, amortization, for purposes of the rules adopted in this proceeding, shall be computed on the straight-line method, *i.e.*, equal amounts shall be recovered in each year of the amortization period. This approach has been applied successfully in common carrier regulation; see 47 CFR § 32.2000(h). Finally, recovery of these costs is permitted only to the extent that they are recorded on the company's books as such. The amortization of allowed start-up losses must begin at the end of the prematurity phase of operation, and should generally be completed during the service life of the longest-lived depreciable assets.

Other losses. The Report and Order concludes that other losses are presumptively excluded from the ratebase: These include continuing operating losses after the system reaches maturity (for these purposes a system reached maturity as defined by FASB 51, *i.e.*, presumptively within two years), and accumulated losses associated with amortization of disallowed goodwill or interest expenses associated with disallowed goodwill. This treatment is appropriate because these costs presumably benefited past subscribers, or were incurred in the expectation of monopoly profits or profits from nonregulated activities, and thus should not be borne by current and future subscribers.

Cable operators have the opportunity of making a showing to overcome this presumption. Such a showing would demonstrate that these costs benefit both current and future ratepayers, and that they were prudently invested in plant that is used and useful in the provision of regulated services. Operators may also present evidence that allowance is necessary to produce compensatory rates.

Treatment of intangibles. The Report and Order addresses the treatment of intangibles in the ratebase. In instances where there is a lack of effective competition, as in the period prior to the adoption of the Cable Act of 1992, the Report and Order finds that acquisition prices are likely to include amounts paid in expectation of supra-competitive profits and growth premiums for unregulated services. Traditional principles of ratemaking and the policies embodied in the Cable Act of 1992 also warrant disallowance of costs that do not represent reasonable costs of providing regulated services to customers, equivalent to the costs that would be incurred under competition. This generally includes acquisition costs recorded as goodwill. The Report and Order makes clear that disallowance of these costs, contrary to some parties' assertions, is not a penalty but part of the normal and proper balancing of the interests of investors and ratepayers.

However, the Report and Order finds that operators are correct in pointing out that some intangible costs do represent cost of providing service that are legitimately included in the operator's ratebase or revenue requirement. This is true whether the operator is an original owner or a purchaser of an established system. Further, such allowance is consistent with the Commission's Part 32 rules, which allow telephone companies to recover intangible costs related to "organizing and incorporating the company, original costs of franchise rights, patent rights, and other intangible property having a life of more than one year." (47 CFR 32.2690). These costs produce assets that provide benefits to subscribers and are reasonably recoverable from subscribers.

To balance investors' and ratepayers' interests fairly, the Report and Order holds that in some cases intangible costs are presumptively allowed in the ratebase. Intangible costs that are generally reasonable costs of providing service, that would be incurred under competition, and that are used and useful in the provision of regulated services, are properly recoverable in rates. In some cases intangible costs may be included in the ratebase; in other cases, they may be treated as an expense, and amortized over a period of years. The Report and Order holds that other intangible costs, including goodwill, will be presumptively excluded.

Organizational costs. The Report and Order finds that organizational costs are presumptively allowed into the ratebase to the extent they are prudently invested and are useful in the provision of

regulated cable service. Organizational costs typically consist of the cost of organizing and incorporating the company. They will ordinarily have been incurred by the entity originally providing cable service in the franchise area in question. These organizational costs should represent costs that benefit customers, in that they must necessarily be incurred for the entity to be able to provide service. See 47 CFR 32.2690. The Report and Order however presumptively disallows from this category stock given to the organizer the value of which is in excess of reasonable salary.

The Report and Order allows operators to continue to recover their capitalized organizational costs based on GAAP through amortization over a reasonable period, subject to scrutiny by the appropriate regulatory authority as to the reasonableness of rates produced by the recovery period. However, the Report and Order notes that it is not necessarily the case that the time period until renewal of a franchise is the appropriate capitalization period for organizational costs, because generally there is an expectation of franchise renewal. Proponents of some period other than the franchise period should support their proposal.

Franchise costs. The Report and Order concludes that the original costs associated with a government franchise are allowed into the ratebase if the costs: (1) Are associated with the costs of winning the franchise; and (2) in the case of purchased systems, are costs that were directly borne by the seller. The Report and Order finds that these costs are presumptively allowed to the extent they are prudently invested and are useful in the provision of regulated cable service. The Report and Order notes that original costs of government franchises are often allowed into the ratebase under traditional cost-of-service principles, because they must necessarily be incurred for the entity to be able to provide service. (See 47 CFR 32.2690). The Report and Order holds that operators will be allowed to continue to recover their capitalized franchise right based on GAAP through amortization over a reasonable period, subject to scrutiny by the appropriate regulatory authority as to the reasonableness of rates produced by the recovery period.

Customer lists. The Report and Order finds that customer lists, too, are presumptively allowed into the ratebase, to the extent that they reflect costs capitalized during prematurity, as defined by FASB 51, and are prudently invested and useful in the provision of regulated cable service. Operators will be allowed to continue to recover these costs through amortization over a reasonable period based on GAAP, subject to scrutiny by the appropriate regulatory authority as to the reasonableness of rates produced by the recovery period.

Acquisition costs. The issue of whether the acquisition costs of cable systems should be considered or accepted for computing ratebases and revenue requirements overlaps to a degree with the question of the plant valuation method that should apply. But the Report and Order emphasizes that the two matters are distinct, especially under the particular circumstances presented by the reimposition of cable service rate regulation by the Cable Act of 1992. Regardless of the valuation method that might be applied now and in the future, the issue cable operators raise is whether the cost-of-service methodology should recognize the prices paid for cable systems in the past, especially during the period when systems were unregulated. The Report and Order concludes that the prices paid for cable systems, especially during the period when those systems possessed market power, are not a reliable or reasonable basis for ratemaking, and that excess acquisition costs, or "goodwill", are therefore from ratebase.

The Report and Order defines "goodwill" as the portion of plant purchase price that cannot be assigned specifically to identifiable property acquired and that is not recorded on the operators' books of account as accumulated losses, subscriber lists, franchise rights, patent rights or organizational costs. The Report and Order concludes that "goodwill," including going-concern value, should be presumptively disallowed from the ratebase because it is likely to represent expectations of supra-competitive profits and other outlays that should not be borne by regulated service customers.

The Report and Order recognizes the importance and controversy that this issue generates, both for operators and customers, because many cable systems changed hands during the years when cable service was essentially unregulated, and in many cases the prices paid exceeded the original cost or the book value of the purchased cable system's tangible assets. These costs to the buyer, termed "excess acquisition costs," are generally recorded as "goodwill". The Report and Order addresses the many arguments made by cable operators for recognition of acquisition costs for computing costs of service. Cable operators claim, variously, that the price paid is either a measure of the fair value of the system, or the proper valuation for assets brought into regulation, or a proper exception to the usual valuation rules to recognize the need for a transition tailored to the characteristics of the cable industry, or a constitutional requirement to prevent confiscation.

The Report and Order sustains the Commission's belief that the prices paid for cable systems, especially during the period when those systems possessed market power, are not a reliable or reasonable basis for ratemaking, and that their use is not required or supported by public utility practice, the purposes of the Cable Act of 1992, or the Constitution. The Report and Order notes that on the FCC's own analysis conducted as part of the development of governing rates set under the benchmark approach, and the study submitted in support of the use of acquisition prices, the Kolbe/Vitka Study, by Viacom, one of the largest cable operators, in reaching the conclusion that acquisition prices often include some expectation of supra-competitive profits that the market power of cable systems operating in a less than fully competitive environment could expect to generate. The Report and Order notes that the magnitude of this expectation probably varied over time, increased by the growing list of cable channels that could be obtained only by subscribing to cable service, and discounted by investors' assessment of the risks of competitive entry and re-regulation. Buyers and sellers negotiating acquisition prices clearly took into account the competitive status of cable systems and their consequent market power. Individual investors purchasing shares in cable companies no doubt also included this factor.

The Report and Order further notes that it is likely that acquisition prices included assessments of the profits that might be gained from emerging cable services that remain unregulated but could be expected to experience more rapid growth and penetration than those services that were made subject to regulation. Premium services such as HBO and Showtime, pay-preview services, interactive services such as home shopping, and other offerings all represent newer sources of profit with greater potential for expansion. System prices can reasonably be expected to include the potential earnings for these actual and planned offerings. Moreover, it is certainly possible that even arm's-length transactions resulted in prices that were simply too high; transactions were based upon overly optimistic projections of growth, the direction of the economy, and the buyer's ability to

reduce operating costs or increase the value to customers. The Report and Order finds that acceptance of these prices as a fair measure of the value of the facilities used to provide regulated services would require customers for those services to act as guarantors of the recovery of those prices, regardless of how inflated they might have been. Such allowance would not be appropriate or reasonable or in the public interest.

The Report and Order points out that traditionally, such excess acquisition costs have been partly or wholly excluded from the ratebase of regulated concerns, because these costs are seen as inappropriate costs for ratepayers to bear. (*E.g.*, 47 CFR 32.2005, 32.2007; *San Diego Land & Town Co.* v. *National City*, 174 U.S. 739, 757–758 (1899); *Simpson* v. *Shepard (Minnesota Rate Cases)*, 230 U.S. 352, 454 (1913)). This is because these costs typically benefit the seller, not the ratepayer; they do not contribute to the plant supporting regulated service. The Report and Order also notes that disallowance of goodwill for monopoly cable systems is consistent with findings of the United States Tax Court in *Tele-Communications, Inc.* v. *Commissioner of Internal Revenue*, 95 T.C. No. 36 (1990).

The Report and Order holds that the decision to disallow acquisition costs, to the extent they include capitalized supra-competitive profits, is consistent with, if not indeed compelled by, the theory and purposes of the Cable Act of 1992. The Act does not instruct the consideration of acquisition costs or the prices individual shareholders paid for cable companies before the adoption of the Act. The language and legislative history of the Cable Act of 1992 demonstrate a primary concern with preventing the undue market power of cable operators subject to neither regulation nor effective competition from setting supra-competitive rates. The Report and Order concludes that allowance of the acquisition price of cable systems as part of the costs of service would present a substantial probability of passing on to customers costs that reflect neither the costs of providing service nor the costs that would be incurred under competition.

Operating efficiencies provide rebuttable presumption. The Report and Order recognizes that there may be sales of cable systems, as some commenters claim, that benefit subscribers by generating operating efficiencies that are unobtainable by the seller. The Report and Order finds that it is appropriate to consider whether these efficiency gains warrant inclusion of some part of the goodwill in the rate calculation. However, in any such case, the Report and Order requires that the operator clearly rebut the presumption against including goodwill by demonstrating the nature and value of the net efficiency gains and, most importantly, that these gains resulted in concrete, tangible benefits to subscribers, especially in the form of better and more varied regulated services. Efficiency gains that permitted the buyer to improve its margins but did not benefit subscribers will not lay the foundation for allowing goodwill to be included in the rates subscribers pay.

The Report and Order requires that operators wishing to overcome the presumption that goodwill is excluded from inclusion in the ratebase demonstrate that allowance of these costs will result in reasonable rates, that the costs are the result of an arm's-length transaction, and that the goodwill has produced for subscribers concrete benefits that would not have been realized otherwise. To the extent that the operator seeks to justify rates above competitive levels based on inclusion of goodwill, there is a heavy presumption against inclusion of these costs. Operators making such a showing will be required to show the nature of each cost they are seeking to justify for inclusion in the ratebase, and should provide all pertinent data relating to the acquisition. At a minimum, this includes the purchase price of plant, its book value, a description of plant, the effect on subscribers, the results of a valuation study, and the results of any request for franchise approval.

The Report and Order provides that in reviewing such showings, the franchising authority or the Commission is to scrutinize the extent to which inclusion of these costs will produce rates above competitive levels. To the extent that they do, the operator will need to demonstrate why its particular situation justifies inclusion of these costs in the ratebase.

Plant under construction. The Report and Order adopts the capitalization method to govern ratemaking treatment of plant under construction. The capitalization method is the traditional method for considering plant under construction. Under this approach, plant under construction is excluded from the ratebase, but the operator calculates an allowance for funds used during construction (AFUDC) and includes this allowance in the cost of construction. As construction is completed and the plant is placed into service, the cost of construction (including AFUDC) is included in the ratebase and recovered through depreciation. This method has been used by various regulatory authorities to provide reasonable rates for utilities. Further, this method will allow operators to recover interest from the construction period only after the plant is placed in service. Interest is to be computed at prime rate or at the operator's demonstrated cost of the funds used for the construction. AFUDC is allowed only to the extent the related costs are not already included in start-up losses.

Cash working capital. The Report and Order adopts a presumption of a zero allowance for cash working capital. The Report and Order finds that cable subscribers are generally billed in advance for regulated cable services, and billed in arrears for nonregulated services such as pay-per-view. Cable operators generally pay vendors, employees, and taxing authorities in arrears. The Report and Order also notes that it is possible, where receipts lead outlays, to establish a negative cash working capital allowance. Given these circumstances, the Report and Order finds it appropriate to adopt a presumption that a zero allowance is needed to support the regulated cable services. A cable operator may rebut the presumption by establishing that its operations do not fit the industry mold, and that it requires the establishment of a cash working capital allowance.

Excess capacity. The Report and Order concludes that operators are allowed to include in the ratebase any excess capacity that will be used within a twelve-month period. As with start-up losses, recovery of these costs is allowed only to the extent that they are recorded on the company's books as such. The amortization of allowed costs must begin at the end of the prematurity phase of operation, and should generally be completed during the service life of the longest-lived depreciable assets. This will generally be no longer than fifteen years.

The Report and Order notes that the price cap adjustment and network upgrade plans (discussed below) make adequate provision for the addition of channels and capacity. Thus, while there is an allowance in the ratebase for any facilities that are not currently used and useful, but will be used and useful within one year, if they are included in the ratebase, they may not in any part be reflected in annual operating expenses or in any price cap adjustment. This will assure that no double or excessive recovery of costs, and no double payment for capacity, can occur.

Cost overruns. The Report and Order determines that cost overruns should be

presumptively disallowed from the ratebase. Subscribers should not bear the burden for unnecessary, extravagant, or imprudent expenses, which cost overruns may be. At the same time, however, the Report and Order recognizes that cable operators should be able to recover the costs of overruns that have occurred through no fault of the operator. Therefore, cable operators may overcome this presumption on a case-by-case basis by showing that the costs were prudently invested. In reviewing such showing, factors that will be considered include whether the overrun was preventable, who was responsible for the overrun, and whether including the overrun in the ratebase will produce reasonable rates.

Premature abandonments. The Report and Order finds that the cost of premature abandonments should be a recoverable operating expense rather than an element in the ratebase. In removing prematurely abandoned plant from the ratebase, a cable operator must bring plant to full recovery before retiring it. Plant that has never entered into service cannot be retired and expensed, but is disallowed. To retire plant, the operator must remove both plant and accumulated depreciation reserve from the balance sheet. Once the plant is retired, an operator may amortize the unrecovered investment (*i.e.*, the original cost less accumulated depreciation) over a term equal to the remainder of the original expected life.

(3) Rules for Determining Recoverable Expenses

Operating expenses. The Report and Order permits recovery of all operating expenses normally incurred by cable operators in the provision of regulated cable service. Thus cable operators may recover fully the reasonable costs of providing regulated service, and subscribers are protected from paying rates that reflect costs not reasonably associated with regulated services. The Report and Order affirms the decision to exclude from recovery those operating expenses and other costs unrelated to the provision of regulated cable service. Generally, costs incurred in the provision of regulated cable service are recoverable if legitimate and reasonable. The Report and Order directs that the Commission and local franchising authorities review operating expenses in each cost showing to assure that they are in conformance with the cost standards.

The Report and Order also adopts the tentative conclusion that certain special expenses (47 CFR 76.924 (f) and (g)) are presumptively excluded from recovery as not reasonably related to the provision of regulated cable services. Cable subscribers should not be responsible for reimbursing cable operators for unreasonable costs. Further, the Report and Order concludes that GAAP should guide the determination of what costs are to be expensed and what capitalized.

Depreciation. The Report and Order declines to adopt the tentative conclusion to prescribe depreciation rates. The Report and Order finds that prescription of depreciation rates is unnecessary, at least pending completion of the cost study and analysis that the Cable Bureau is to undertake. See, FNPRM elsewhere in this **Federal Register**. Further, the Report and Order finds that a depreciation prescription requirement would impose unjustified burdens without providing a balancing benefit to subscribers. Instead, the Report and Order directs regulators to monitor industry depreciation practices closely, and to review depreciation showings in individual cost proceedings carefully to assure that these depreciation practices are reasonable. In addition, the Report and Order notes that the Commission and local franchising authorities will examine depreciation practices of operators in individual cases to assure that resulting rates are reasonable.

Taxes. The Report and Order develops a method of income tax treatment that permits recovery of income taxes regardless of the form of ownership of the regulated cable service enterprise. The Report and Order maintains the principle that taxes related to the provision of regulated service may be recovered from subscribers, but taxes on dividends paid to owners may not. The Report and Order affirms the tentative conclusion that Chapter C corporations will be allowed to include in annual expense calculations all taxes on the provision of regulated cable service. For other ownership forms of cable operators—subchapter S corporations, partnerships, sole proprietors—the income tax allowance is to be determined as follows: The permitted rate of return on the ratebase is first calculated; this amount is adjusted to remove any portion of the previous year's distributions after adjustment for capital contributions and interest paid; the resulting sum, the amount retained in cable operations, will constitute the cable operator's earnings subject to the income tax calculation. The allowed income tax will be calculated by applying the grossed-up federal and state statutory corporate tax rates (as opposed to individual tax rates) to the amount calculated as subject to the income tax calculation, regardless of the actual business form. The calculated tax amount may then be included in calculating the total revenue requirement.

The Report and Order notes that while traditional cost-of-service regulation allows for recovery of allowable tax expense on an annual basis, it is possible that cable rates set by cost of service will not be reviewed, nor any further cost support submitted, for a substantial period of time. Retained earnings depend closely upon the cable system's current financial requirements. Because this is a showing the Commission does not intend to revisit, proposed tax expense in a cable cost-of-service showing should incorporate an adjustment of retained earnings to reflect likely changes. The following illustration of tax calculation methodology adjusts retained earnings over a three-year period:

	Year 1	Year 2	Year 3
1. Ratebase	1000000	1000000	1000000
2. Allowed Return (@ 11%)	110000	110000	110000
3. Less Interest Expense	(10000)	(10000)	(10000)
4. Tax Gross-up:			
5. Allowed Taxable Return	100000	100000	100000
6. Distributions	50000	25000	160000
7. Capital Contributions	0	25000	10000
8. Amount Subject to Tax calc.	50000	100000	(50000)
9. Tax allowed at corp. rate (@ estimate 34% grossed up)	25758	51515	(25758)
10. Revenue Requirement:			
11. Allowed Return	110000	110000	110000
12. Tax Allowed	25758	51515	(25758)
13. Expenses	500000	500000	500000

	Year 1	Year 2	Year 3
14. Total Revenue Requirement	635758	662515	584242
15. Cumulative Tax Allowed:			
16. Beginning Balance	0	25758	77273
17. Current Provision	25758	51515	(25758)
18. Ending Balance[6]	25758	77273	51515

[6] Explanation of terms and calculations:
1. Line 3: An eleven percent rate of return is used only for purposes of illustration.
Line 6: A portion of distributions made must be associated with the provision of regulated cable services.
Line 7: A portion of contributions made must be associated with the provision of regulated cable services.
Line 8: Tax allowed is determined by subtracting distributions from allowed return and adding the amount of capital contributions. The amount of contributions added shall be no more than the amount of distributions for the period, however.
Line 9: The rate used in this illustration is a federal tax rate grossed up as follows: (.34/(1−.34))=.51515)
2. Lines 8–9 of Year 3 demonstrate that, where distributions offset the total of allowed return and capital contributions, the amount subject to the tax calculation may be negative. In effect, this calculation would require operators to pay back to subscribers the tax benefits associated with earnings that had been achieved previously but were distributed in the current period. Since no annual adjustment will be made, this offset should be reflected in an operator's one-time showing.

The Report and Order does not require the three-year calculation shown above. However, it does require that cost-of-service showings that include a tax allowance show some calculation of likely changes in retained earnings.

The Report and Order also adopts the Commission's tentative conclusion that cable operators may include state and federal taxes, such as property and sales taxes, incurred on the provision of regulated cable service as an operating expense regardless of business form.

Test year methodology. The Report and Order adopts the use of an adjusted historic test year. The test year may be adjusted for "known and measurable" changes that have occurred by the time the rates take effect. The Report and Order further finds that the historic test year should be the operator's fiscal year. Thus, cost-of-service showings must be based upon the operator's most recently completed fiscal year. In the case of a cost-of-service showing arising in response to a complaint, the fiscal year should be the one most recently completed at the time of the filing of the complaint. In the case of new systems, for which no historic data are available, projected data may be used, but careful scrutiny shall be paid to the assumptions used.

(4) Use of Unitary 11.25% Rate of Return

A major component of the ratemaking methodology for cable operators that elect cost-of-service regulation is the rate of return those operators will be given an opportunity to earn on their allowed ratebase. The Report and Order prescribes an interim, overall rate of return of 11.25% for use in cable cost-of-service proceedings.

Uniform rate of return. The Report and Order finds that the record confirms that the burden of establishing an individualized rate of return for each cable operator that elects cost-of-service regulation would be substantial. Such an undertaking would require cable operators to present, and franchising authorities or the Commission to review, analyses of matters such as the risks individual cable systems encounter in providing regulated cable service and the sources of capital available to finance those risks. Not persuaded that it is necessary for cable operators and regulators to undertake such analyses to ensure that cable operators can attract the capital needed to provide regulated cable service, the Report and Order defines a uniform rate of return for use by all cable operators in cost-of-service showings.

Presumptive. The Report and Order acknowledges that some cable operators may believe that the overall rate of return is inadequate to compensate them for the risks they encounter in providing regulated cable service. Similarly, consumers may find this overall rate excessive, given the individual operator's specific circumstances. To ensure the reasonableness of all rates set in cable cost-of-service proceedings, the Report and Order states that parties to such proceedings are not foreclosed from attempting to justify different rates of return. Parties that seek rates of return different from the prescribed interim rate of return, or any subsequently prescribed rate of return, bear a heavy burden. In particular, each cable operator seeking a higher rate of return is required to show exceptional facts and circumstances that make its cost of capital for regulated cable services exceed the prescribed rate of return, and must demonstrate that those facts and circumstances will persist. All necessary supporting information shall be included in the challenging cable operator's initial cost-of-service showing. Similarly, local franchising authorities may collect and consider evidence that the operator's cost of capital for the individual system is lower than the prescribed rate. The Commission will review all evidence relied upon by local franchising authorities in setting rates of return different from the prescribed rate.

General methodology. The Report and Order determines to use the weighted average cost of capital as the methodology for establishing the rate of return. The Report and Order describes in detail each of the components: Cost of equity, cost of debt, and capital structure. This weighted average cost of capital approach assumes a post-tax return on equity.

In applying this methodology, an estimate of the cost of the capital contributing to the provision of regulated cable service is required, since most cable companies have diverse operations. The record provided no company which engaged only in provision of regulated cable service. Thus, the Commission selected surrogate firms to represent the risks of regulated cable for capital analysis.

The Report and Order notes that the surrogate firms must operate a levels of risks comparable to those of regulated cable service in order to be consistent with the fundamental goal of determining the return required to compensate investors for the perceived risks of regulated cable service and to attract capital to that service. In choosing surrogate firms, recognition is given to the limitations imposed by the available information. Because different kinds of information are available with regard to cost of equity, cost of debt, and capital structure, each of these components of the overall cost of capital is addressed separately.

Cost of equity. The Report and Order espouses the principle that the ideal cost of equity estimate should accurately reflect investor expectations as to the returns, in terms of both capital gains and dividends, investors will earn. Since investor expectations are not directly measurable, a variety of indirect methods are used. The Report and Order

reviews the methods used by commenters in this proceeding, which fall into three categories: risk premium, discounted cash flow (DCF), and comparable earnings. Commenters submitted four studies, using the capital asset pricing model (CAPM) version of the risk premium method, one study relying upon the DCF method to analyze the Standard & Poors 400 (S&P 400), and one applying the comparable earnings methodology. In Attachment D to the Report and Order, these three methods of estimating the cost of equity are described and analyzed.

The Report and Order concludes that the DCF methodology will be applied to the S&P 400 to develop the cost of equity for companies providing regulated cable service. The Report and Order and the separate attachment present the basis for rejecting commenters' arguments against use of the DCF methodology and against the use of the S&P 400 as a surrogate, and rejects other approaches suggested in the cost of equity studies by commenters. Thus, the Report and Order affirms the tentative proposal in the Notice to apply the DCF method to the companies composing the S&P 400. (*Notice* at ¶ 52).

The DCF method, like the other methods the parties advocate, requires an assessment of the risks of regulated cable service in comparison to those of the chosen surrogate. The record provides little definitive analysis of the risks of regulated cable service and thus does not make clear which specific subgroup of the S&P 400 regulated cable most resembles in terms of risks. Given the paucity of the record, the Report and Order determines that the S&P 400 should be viewed broadly and a broad zone of reasonableness for the cost of equity should be defined. Based on the Vander Weide analysis, estimates for the cost of equity for regulated cable service are between 11.80% (the midpoint of the DCF cost of equity estimates for the first quartile of the S&P 400) and 15.11% (the midpoint of the DCF cost of equity estimates for the third quartile). The Report and Order finds that these estimates provide reasonable outside bounds for the cost of equity for regulated cable service, approximately 12% and 15%. The Report and Order adopts use of this range, in combination with other elements of the weighted average cost of capital, to develop a zone of reasonable rates of return for regulated cable service.

Cost of debt. The record on the cost of debt includes compilations of debt costs for specific cable operators. The information is both industry-specific and concrete. The Report and Order concludes that it appropriate to rely on this information, instead of S&P 400 data, as a surrogate for the cost of debt for regulated cable service, because it is industry-specific and provides a sufficient basis for estimating that cost of debt. Thus, the tentative conclusion to rely on the cost of debt of the surrogate is rejected.

The cost of debt found by Vander Weide for six cable companies was 7.8%. AUS found an 8.5% cost of debt based on 1992 data and notes it would be lower with more recent data. Several parties suggest higher debt costs, but provide no supporting documentation. Adelphia's SEC Form 10K for 1993 states that its floating note interest rates ranged from LIBOR plus 1.0% to LIBOR plus 1.5%. Its March 31, 1993 average debt rate was 8.65%. TCI's SEC Form 10K for 1991 states 55% of its debt was fixed rate, with an average cost of 9.9% and 45% percent was variable rate, floating at the prime rate. The prime rate on February 18, 1994, was 6% and LIBOR was 3.56% (90 day) and 3.75% (180 day).

The Report and Order computes the range for the average cost of fixed rate debt established by this information for the most recently available period (1992–93) as 7.8% to 8.65%. The Report and Order determines that the reasonable estimate of the cost of debt for cable is 8.5%. In addition to reflecting historical debt costs, this rate allows for an increase in the cost of floating rate debt above current rates.

Capital structure. The Report and Order addresses the recommendations of commenters that provided analysis of the capital structure for the cable industry as requested in the Notice. The Report and Order notes the difficulty encountered in evaluating current cable industry practices. The Report and Order evaluates the proposals for establishing a capital structure and discusses in detail the problems arising with each proposal. The Report and Order further notes that the long-term average capital structure of the industry is not clear at this time. Thus, instead of adopting a single capital structure, the Report and Order finds that a capital structure range, for use in the determination of the overall cost of capital for regulated cable operations, is appropriate. Based on the record, the Report and Order determines that a wide range of capital structures, extending from 40% debt to 70% debt, is justified, and is consistent with the range for cost of equity estimates and the cost of debt.

Overall cost of capital. The Report and Order reviews recommendations for establishing an overall cost of capital, and reflects on requirements of The Cable Act of 1992 that the cable rate regulations provide cable operators the opportunity to earn "a reasonable profit" while "protecting subscribers * * * from rates * * * that exceed what would be charged * * * if such cable system were subject to effective competition." 46 U.S.C. 623(b)(2)(C)(vii) and (b)(1), respectively. Companies regulated under this standard must be allowed an opportunity to earn a return sufficiently high to maintain financial integrity and attract new capital. At the same time, the prescribed return must not produce rates that are unreasonable. The courts have recognized that there is a zone of reasonableness within which reasonable rates may fall, and that regulatory agencies have broad discretion to select a return within that zone.

Given this standard, the Report and Order develops its determination of a reasonable range for the cost of equity for regulated cable service, cost of debt, and a reasonable range for the capital structure. The following table combines all these elements and presents the overall cost of capital implied by these ranges.

CALCULATION OF OVERALL RATE OF RETURN DEBT PORTION OF CAPITAL STRUCTURE

	In percent			
	40	50	60	70
Equity estimate (in percent):				
12	10.6	10.3	9.9	9.6
13	11.2	10.8	10.3	9.9
14	11.8	11.3	10.7	10.2
15	12.4	11.8	11.1	10.5
Average	11.5	11.0	10.5	10.0

Debt Cost: 8.50 percent.

No particular weight is given to any one cell in this table. Instead, consideration is given to the averages that are produced, as shown on the last row. Based on these averages, the Report and Order finds that the overall cost of capital for regulated cable service lies within a "zone of reasonableness" of 10.0% to 11.5%.

The Report and Order notes the concerns in selecting a rate within this zone, since the record is less than perfect. Also, the risks of regulated cable operations are not known with certainty, since those risks are dependent in part on the cost-of-service rules and principles adopted in this Order and on the revised benchmark methodology. Additionally, there is a recognized desire to encourage

infrastructure development. Thus, the Report and Order determines that prescribing a return toward the upper end of the zone of reasonableness will enable cable operators to attract the capital needed to provide regulated cable service and to expand their regulated offerings. Based on these considerations, the Report and Order prescribes an overall cost of capital of 11.25%.

Interim rate. The Report and Order notes that the rate of return prescription is an interim one. The FNPRM (published elsewhere in this **Federal Register**) seeks information on the relative risks of cable operations given recent actions by the FCC, and further analysis of S&P 400 companies' costs of capital.

(5) Accounting and Cost Allocation Requirements

Existing requirements. Under existing rules, regulated cable operators are required to maintain their accounts in accordance with GAAP. 47 CFR 76.924(b). They are also required to maintain their accounts in a manner that will allow for identification of appropriate costs and application of cost assignment and cost allocation procedures necessary for rate adjustments to reflect changes in external costs and for cost-of-service showings. 47 CFR 76.924(c). In addition, for accounting purposes, cable operators are generally required to aggregate expenses and revenues at either the franchise, system, regional or company level in a manner consistent with the practices of the operator as of April 3, 1993. 47 CFR 76.924(d). (The initial rules erroneously identified this date as April 3, 1992. The rules adopted with this Report and Order correct this error). Costs associated with franchise fees, franchise requirements, local taxes, and local programming must be identified at the franchise level. *Id.*

Interim summary level accounts. The Report and Order adopts an interim summary accounting system for use by cable operators that elect cost of service regulation. This interim summary account system will be required until a permanent system of accounts is in place. Cable operators that elect cost of service regulation shall identify costs in 55 summary level accounts contained in FCC Form 1220. This form requires that cost-of-service showings include a balance of broad summary level investment, expense, and revenue categories.

The Report and Order expresses concern that even this summary accounting approach may be burdensome for some small systems. In order to provide further relief to small systems, the summary level of accounts that small operators are required to report as a part of the cost of service filings are aggregated further. The Report and Order thus, adopts the requirement that small cable system operators may identify their costs in FCC Form 1225, which contains 32 summary level accounts.

Filing instructions. With regard to the level at which these accounting requirements apply, the Report and Order requires that cable operators electing cost-of-service regulation identify all amounts associated with each revenue and cost category, as provided for in FCC Forms 1220 and 1225, at the franchise, system, regional and/or company level, depending upon the organizational level at which the operator identified revenues and costs for accounting purposes as of April 3, 1993. (§ 76.924(c)). The FNPRM (published elsewhere in this **Federal Register**) will provide for cost studies to explore the extent to which operators should be permitted or required to report average costs at levels different than those in effect on April 3, 1993.

Further, the Report and Order requires cable operators to provide any additional financial data and explanations reasonably requested by franchising authorities and the FCC to substantiate cost-of-service showings or other related proceedings. Where a reasonable response is not forthcoming, franchising authorities and the Commission are authorized to make such disallowance as are appropriate, pending the presentation of convincing evidence by cable operators.

Cost allocation requirements. The Report and Order finds that it is necessary to require allocation of costs to nonregulated service categories to help ensure that the allocation of costs to regulated services is fair and reasonable in relation to the allocation of costs to nonregulated services. The current rules require that costs be allocated among the basic service tier and each tier of cable programming service. 47 CFR 76.924(e)(2). The Report and Order amends the rule to require that, in addition to the basic and cable programming service tiers, cable operators shall allocate costs to nonregulated programming service activities, other cable activities, and non-cable activities.

The Report and Order requires that, after revenues and costs are identified at the appropriate organizational level(s), cable operators shall allocate costs among the equipment basket (47 CFR 76.923(d)) and the following service cost categories: Basic service, cable programming services, nonregulated cable programming services, other cable activities and non-cable activities. These allocations shall be used for cost-of-service showings and for allocating external costs. For the purpose of allocating their costs and revenues among the service cost categories and the equipment basket in cost-of-service proceedings, cable operators shall use FCC Form 1220 or FCC Form 1225 (for use by small cable system operators).

The Report and Order also requires direct assignment of all costs, to the extent possible, among the equipment basket and the service cost categories. Direct assignment applies when costs are incurred exclusively to support the equipment basket or a specific service cost category. For example, most programming charges from program suppliers relate to specific programming. Those charges should therefore be directly assigned to the tier on which the programming is offered. In making this determination, the Report and Order modifies the existing requirement that, with a few exceptions, cost categories identified at the franchise level be generally allocated to the basic tier based on the ratio of channels in the basic tier to the total number of channels offered in the franchise area, and that costs allocated to each tier of cable programming be based on the ratio of channels in each cable programming services tier to the total number of channels offered in the franchise area. The Report and Order finds that when direct assignment is possible, it is preferable to a standard allocator because, while cost allocation provides an estimate of the origination of certain costs, direct assignment is simpler to apply, and more accurately reflects cost causality.

The Report and Order requires that cable operators allocate among the service cost categories and the equipment basket any costs that cannot be directly assigned, using methodologies that are consistent with the procedures in § 76.924(f)(5). These procedures require that, when direct assignment is not possible, operators must first attempt to allocate costs through direct analysis of their origin. 47 CFR 76.924(f)(5)(i). Where direct analysis is not possible, operators must attempt to establish cost-causative linkage to other costs directly assigned or allocated by direct analysis. 47 CFR 76.924(f)(5)(ii). Finally, where no direct or indirect linkage can be made, operators are required to allocated on the basis of the totals of all costs directly assigned and allocated using direct assignment, direct analysis and indirect linkage. 47 CFR 76.924(f)(5)(iii). The

Report and Order requires the Commission and local franchising authorities to review the allocators proposed by cable operators on a case-by-case basis to determine whether the allocators achieve reasonable results.

The Report and Order maintains the current requirement that cable operators allocate costs that were identified at higher levels to the franchise level on the ratio of the total number of subscribers at the franchise level to the total number of subscribers served at the higher level. 47 CFR 924(e)(1). The Report and Order amends the rule, however, to specify the particular procedures that must be followed for allocating costs to the franchise level. First, recoverable costs that have been aggregated at the highest organizational level at which costs have been identified are allocated to the next (lower) organizational level at which recoverable costs have been identified on the basis of the ratio of the total number of subscribers served at the lower level to the total number of subscribers served at the higher level. Second, this procedure is repeated at every organizational level at which recoverable costs have been identified, until all costs have been allocated to the franchise level.

(6) Accounting and Cost Allocation Requirements for External Costs

Definition. External costs are categories of costs that cable operators may pass through to subscribers without a cost-of-service showing under our price cap rules. Such costs include retransmission consent fees, other programming costs, taxes, franchise fees, and costs of other franchise requirements. See § 76.922(d)(3).

Treatment for rate adjustments. To provide for a readily ascertainable basis for proposed external cost adjustments, the accounting and cost allocation rules adopted in this Report and Order will apply to external cost calculations. The Report and Order requires that the following external costs be identified at the franchise level: Franchise requirements, franchise fees, local taxes and local programming. Cable operators are required to identify all other external costs at the franchise, system, regional and/or company level, depending upon the organizational level at which they identified costs for accounting purposes as of April 3, 1993. These costs shall be identified on FCC Form 1210. After external costs have been identified at the appropriate organizational level(s), cable operators are required to allocate such costs among the service cost categories and the equipment basket in the manner specified for cost-of-service showings.

With respect to the specific requirements for allocating certain external costs, the Report and Order requires that the costs of programming and retransmission consent be allocated to the service cost category on which the signal or programming is offered. The phrase "*tier*" on which the programming or broadcast signal at issue is offered" is replaced with the phrase "service cost category in which the programming or broadcast signal at issue is offered." See § 76.924(f)(1) (emphasis added). The Report and Order also requires that the costs of public, educational, and governmental access channels carried on the basic tier be directly assigned to basic service cost category where possible. The Report and Order modifies the allocation requirements for franchise fees. Under the current rule, "franchise fees shall be allocated among equipment and installations, program service tiers and subscribers in a manner that is most consistent with the methodology of assessment of franchise fees by local authorities." Consistent with the treatment of § 76.924(f)(1), the phrase "program service tiers" is replaced with the phrase "service cost categories." See § 76.924(f)(2). While the franchise fee should be allocated among the equipment basket and the service cost categories as the rules currently require, the rules should not list subscribers as a category to which such costs should be allocated. The equipment basket and the service cost categories are the only appropriate categories for allocation purposes. As already noted, the cost of franchise fees must be identified at the franchise level.

The Report and Order also modifies existing rules to require that, to the extent possible, all external costs be directly assigned among the service cost categories. When direct assignment is possible, it is preferable to a standard allocator because it is simpler to apply and it more accurately reflects cost causality. For those external costs that cannot be directly assigned, the Commission requires that cable operators propose specific allocators that reasonably allocate costs among the service cost categories and the equipment basket. The Commission and franchising authorities shall review the allocators proposed by cable operators on a case-by-case basis and determine whether the allocators achieve reasonable results.

For the purpose of establishing external costs at the franchise level, the Report and Order retains the current requirement that cable operators allocate costs that were identified at higher levels to the franchise level on the ratio of the total number of subscribers at the franchise level to the total number of subscribers served at the higher level. However, the Report and Order amends the rules to specify the particular procedures that must be followed for allocating costs to the franchise level in the case of adjustments to external costs as well as cost of service regulation.

(7) Requirements for Affiliate Transactions

The report and Order adopts rules for affiliate transactions that will apply to cable operators who either elect cost-of-service regulation or seek to adjust benchmark/price cap rates for affiliated programming costs. For those operators electing to use the benchmark/price cap approach, the affiliate transaction rules will only be applicable to affiliate transactions involving programming. In Docket No. 92–266, under price caps, cable operators may pass-through affiliated programming costs that exceed inflation as long as the prices charged to the affiliated cable system operators reflect either prevailing company prices offered in the marketplace to third parties (where the affiliated program supplier has established such prices) or the fair market value of programming. First Order on Reconsideration at ¶ 114.

Under the rules adopted in the Report and Order, cable operators that elect cost-of-service regulation or who seek to adjust benchmark/price cap rates for affiliated programming costs shall be required to apply valuation methods that are similar to those telephone companies are now required to apply. Although the rules for telephone companies specify the manner of accounting for affiliates transactions, the affiliate transaction rules adopted for cable operators in this Report and Order do not impose accounting requirements. The affiliate transaction rules adopted with this Report and Order merely set the limits for inclusion of investment and expense in rates set on a cost-of-service basis. They will also govern external cost treatment of programming cable operators purchase from affiliates. These methods distinguish between asset transfers and the provision of services.

When a cable operator sells assets to an affiliate or buys assets from an affiliate, the assets shall be valued at the asset provider's prevailing company price, if the provider has sold the same kind of asset to a substantial number of third parties at a generally available price. Absent a prevailing company price, the cable operator shall value the

asset at the higher of net book cost and estimated fair market value when the regulated cable system is the seller, and at the lower of net book cost and estimated fair market value when the regulated cable system is the buyer.

When a cable operator sells services to an affiliate or buys services from an affiliate, the services shall be valued at the provider's prevailing company price, if the provider has sold the same kind of service to a substantial number of third parties at a generally available price. When the provider has established no prevailing company price, the cable operator must value the service at the service provider's cost.

In determining the prevailing company price, the Report and Order requires that it be based on the price at which the provider has sold the same kind of asset or service to a substantial number of third parties at a generally available price. In determining the cost of both assets and services, cable operators shall apply the costing methods and the rate of return adopted in the Report and Order for cable cost-of-service showings, to the extent applicable, and shall otherwise use reasonable costing methods. Where there is no prevailing company price, affiliate transactions must be carefully scrutinized to ensure that costs are calculated accurately and, for asset transfers, that fair market value is estimated properly. Therefore, cable operators must be prepared to demonstrate that any affiliated transactions costs they claim as regulated costs reflect the cost-of-service methodologies adopt with the Report and Order.

For the purpose of evaluating affiliate transactions that involve programming, the Report and Order determines to classify programming as an asset. Hence, for the purpose of establishing initial costs for programming purchased by a cable operator from an affiliate, the cost of the programming shall equal the provider's prevailing company price, if the provider has sold the same kind of programming to a substantial number of third parties at a generally available price. Absent a prevailing company price, the cost of the programming shall equal the lower of the provider's net book cost and the programming's estimated fair market value. Except to the extent that they are relevant for estimating fair market value, the Report and Order does not allow for the establishment of affiliate prices by reference to the prices independent suppliers charge third parties for the same or similar products.

The Report and Order applies the rules adopted in the program access proceeding to define affiliated programmers. Rate Order, 8 FCC Rcd at 5788, n.601, citing Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition and Diversity Act of 1992—Development of Competition and Diversity in Video Programming Distribution and Carriage, Report and Order, FCC 93–178, 58 FR 27658, released May 11, 1993. Under those rules, an affiliated programmer is a programmer with an ownership interest of five percent or more, including general partnership interests, direct ownership interests, and stock interests in a corporation where such stockholders are officers or directors or who directly or indirectly own five percent or more of the outstanding stock, whether voting or nonvoting. Such interests include limited partnership interests of five percent.

The Report and Order requires cable operators to provide detailed disclosure of affiliate transactions so that the Commission and franchising authorities can ensure that affiliate transactions are treated consistent with the limits of this Report and Order. Where cable operators have not demonstrated that their affiliate transactions meet the requirements of the affiliate transaction rules, disallowances shall be made by the Commission and franchising authorities.

(8) Streamlined Filing and Review for Small Systems

The Report and Order acknowledges Congress' directive under the Cable Act of 1992 to reduce the administrative burdens of, and costs of compliance with, cable regulations for small cable systems. 47 U.S.C. 623(i). The Report and Order adopts an abbreviated cost of service form for use by small systems, Form 1225. This will reduce the administrative burdens of cost showings for small system operators, while retaining the necessary regulatory oversight and assurance of reasonable rates. The Report and Order further requires that information provided on the abbreviated cost of service form be certified by the operator as correct; it will be subject to audit by the local franchising authority and by the Commission.

Independent small systems and small systems operated by small MSO's may use Form 1225. Small MSO's are those multiple system operators that (1) Serve 250,000 subscribers or less, (2) own only small systems with less than 10,000 subscribers, and (3) have an average system size of 1,000 or fewer subscribers. This is the same standard of eligibility that the Commission adopts for other small system administrative relief in the Benchmark/price cap Order, which is summarized elsewhere in the **Federal Register**.

However, The Report and Order does not allow use of this form for small operators affiliated with larger systems. The Report and Order adopts the same affiliation standards employed for small system administrative relief generally. Use of the small system relief form (Form 1225) is not permitted by companies in which a larger company holds more than a 20 percent equity interest (active or passive) or over which a larger company exercises actual working control (such as through a general partnership or majority voting shareholder interest). This affiliated standard also governs eligibility for the use of the abbreviated summary level accounts for small systems.

Finally, the Report and Order notes that while all cable companies that choose to make cost-of-service filings should be subject to the uniform accounting requirements as proposed here, at least in abbreviated form, such accounting requirements may increase the administrative burden on small operators to the point of hardship, and small operators may be unlikely to require the same level of regulatory oversight as larger entities. Thus, in our Further Notice, comment is sought on whether to exempt small systems and/or small operators from these requirements entirely. The Commission also is adopting reduced accounting requirements for small systems.

(9) Streamlined Filing Requirements for Network Upgrades

The Report and Order concludes that an abbreviated cost-of-service showing for network upgrades, with safeguards, provides an appropriate way to implement the goals of the Cable Act of 1992, to promote the availability of diverse cable services and facilities, encourage economically justified upgrades, and reduce regulatory burdens, while ensuring reasonable rates for regulated services.

The Report and Order notes that for many systems, this option will be unnecessary or inapplicable. The benchmark/price cap mechanism is already based on the rates of competitive systems, including those with upgraded networks. The rates charged by those systems presumably recover their capital costs. The benchmark also includes factors reflecting the number of channels a system furnishes to customers. Nevertheless, there may be cases where the benchmark rates do not provide sufficient revenue to attract capital for

upgrades because of unusual costs associated with capital improvements. For these cases the abbreviated cost-of-service showing should provide the ability to attract the capital needed for the upgrade.

The abbreviated cost of service showing for network upgrades is available only for significant upgrades requiring added capital investment, such as expansion of band width capability and conversion to fiber optics, and for system rebuilds. Normal improvements and expansions of service will remain subject to the usual rate review process. The Report and Order finds that to justify an increase in the rates for regulated services, the operator will be required to demonstrate that the capital investment actually will benefit subscribers through improvements in the regulated services subject to the rate increase. The Report and Order also holds that, except to the extent provided by our AFUDC policy, the upgrade rate increase should not be assessed on customers until the upgrade is complete and providing these benefits to customers of the regulated services. This is consistent with the general cost-of-service standard that only used and useful property should be included in the ratebase. Any costs that are not used and useful, will be deducted from total cost. Issues of allowable costs can be resolved if raised by comparison with costs of similar systems and, in particular, systems subject to competition.

To assure that the upgrade rate increase is justified by higher costs, the Report and Order requires that the operator bear the burden of demonstrating the amount of the net increase in costs, taking into account current depreciation expense, likely changes in maintenance and other costs, changes in revenues, and expected economies of scale. The Report and Order requires that the operator must also allocate the net increase in costs in conformance with the cost allocation rules for cost-of-service showings, to assure that only costs allocable to regulated services are imposed on subscribers to those services.

The Report and Order explains that the permitted rate (based upon the showing of the net increase in allowable costs associated with the capital improvement) would be provided in two elements. The first element is the benchmark rate, as governed by the Rate Order and the price cap. The second element is the capital improvement add-on. The sum of these two elements yield the maximum allowable rate that might be charged to subscribers. The capital improvement add-on is not adjusted for inflation but is a fee charged over the useful life of the improvement determined in accordance with our cost-of-service requirements.

The Report and Order delegates to the Cable Services Bureau the development of appropriate forms for these abbreviated showings.

(10) Hardship Rate Relief for Operators

The Report and Order recognizes that, in extraordinary cases, the cable industry may face special problems as it moves into a regulated environment, and that it is conceivable that the particular circumstances of an operator could be such that the practical result of applying any of these rate options could still be to threaten the financial health of the operator and its continued ability to provide cable service.

The Report and Order addresses this possibility, and notes that the Commission will consider the need for special rate relief for operators in individual cases. To demonstrate eligibility for such extraordinary relief, the operator should establish that the rates permitted by the benchmark/price cap and cost-of-service mechanisms undermine the financial health of the operator so that it is unable to attract capital and maintain credit necessary to operate, despite prudent and efficient management. The operator should also establish that the resulting rates, though higher than those justified by the operator's costs, will nevertheless not be unreasonable or exploitative of customers. For example, the operator should demonstrate that the rates are not excessive in comparison with similarly situated systems, particularly systems subject to competition.

The Report and Order requires that this hardship showing must be made for the MSO level, or in any event at the highest level of the operator's cable system organization. The operator should provide all information and legal authority on which it seeks to rely, and all factors it believes the Commission should consider, to demonstrate that the end result of the other ratesetting options available to it would place the operator in financial difficulty warranting rate relief, and that on balance this relief would not result in unreasonable rates for customers. If the operator makes an adequate initial showing of facts which, if proved, might warrant rate relief, the Commission will subsequently provide the operator with an opportunity to prove the facts alleged and demonstrate that, balancing the relevant interests of investors and ratepayers, rate relief is warranted.

(11) Experimental Upgrade Incentive Plan

The Report and Order determines that the goal of promoting economically justified system upgrades, as well as the goals of the Cable Act and of this proceeding, would be furthered by development of an incentive regulation approach to upgrading cable services, similar to the incentive plans implemented for telephone carriers. The Report and Order outlines the incentive approach as follows. Basically, an operator would be permitted to enter into a "social contract" with its customers under which the operator would be given substantial flexibility in setting rates for new regulated services it introduces, such as new service tiers offering additional program channels. In exchange, customers would be guaranteed that rates for current services would be kept stable and reasonable, no higher than rates before the contract takes effect or the benchmark/price cap rate (which might include adjustments for inflation and external cost changes), and that this would purchase at least the same program channels, or channels of equivalent value to customers. The operator would also commit to otherwise maintaining or improving its service quality. The contract would be effective for a term of years and would be overseen by this Commission, and reviewed before the end of the term.

The Report and Order notes that a plan such as this, which protects the rates and quality of current cable service tiers, while providing profit incentives for operators to introduce new and improved regulated services, may help carry out the purposes of the Cable Act while also being fair to customers of current services, less burdensome on cable operators and those responsible for their regulation, and more likely to encourage worthwhile investments to upgrade cable service.

The Report and Order contemplates that this plan will generate a strong incentive for the operator to undertake only upgrades that are economically justified and that best meet customer needs, and to make such upgrades in the most efficient manner possible. In order to profit from the planned upgrade, an operator must provide customers with additional or upgraded services they want to buy. Marketplace forces, not this Commission, will determine which services succeed. A properly designed incentive plan for system upgrades should help achieve other goals. It should, for example, help encourage operators to provide additional tiers of services. An incentive regulation plan should also reduce regulatory burdens,

even below those likely under the add-on rate proposal. Regulatory review should only encompass whether the operator is continuing to offer existing services at rates no higher and quality no lower than the operator contracted to provide. The Commission would not expect to investigate complaints regarding rates for additional regulated services unless they were clearly outside a wide range of reasonable rates, as evidenced, for example, by similar systems.

Offering substantial rate flexibility may also be appropriate to encourage operators to take the entrepreneurial risk of investing in the upgrades needed to offer such services, while replicating competitive marketplace forces. In competitive markets, entrepreneurs offering new and improved services can hope to reap above-market profits for some period, at least until competitors catch up, but also take the risk that the services will not succeed in the marketplace. Permitting cable operators to take the risks and to keep the rewards of introducing new and improved services, at least for a reasonable period, should have similar benefits when applied to cable operators.

The Report and Order notes that additional services will be indirectly regulated by the price cap on current regulated services. The added services and capabilities must effectively compete with the other regulated services, whose rates are limited by regulation. Customers are likely to subscribe to and pay for the added services and capabilities only if they offer additional value at a reasonable price, in comparison to those offered by current tiers.

The Report and Order observes that to generate an incentive plan that is effective in encouraging operators to invest in worthwhile upgrades, but also fair to customers, the rate limits on existing services and the rate flexibility for new services would apply for a substantial period, but would be subject to eventual review. For instance, in the case of telephone companies, an initial review is made during the fourth year of the price cap incentive plan. In view of the initial start-up issues for any incentive plan for cable operators, a longer period is probably desirable, both to permit operators to understand and respond to the plan and to assure strong efficiency incentives. Thus, the Report and Order proposes that the Commission review the plan in the fifth year of operation.

The Report and Order adopts the Upgrade Incentive Plan on an experimental basis. Cable systems that commit to meet the basic obligations of freezing rates for current services that have been adjusted to benchmark/price cap or cost of service levels, or conforming their rates to the price cap, and maintaining programming and service quality that is at least as valued by customers as that offered currently, will be permitted substantial rate flexibility in the rates they might wish to introduce for additional regulated services and capabilities for a term of years, up to five years, from the acceptance of the plan. These experimental plans will then be monitored and reviewed no later than the fifth year to evaluate their performance.

To gain experience with this approach, the Report and Order states that the Commission will consider proposals from cable operators that will implement the Upgrade Incentive Plan on an experimental case-by-case basis, for a limited term of years. Cable operators wishing to participate should submit a proposal to the Commission's Cable Services Bureau outlining a proposal and explaining how it would implement the objectives outlined here. The proposal should also be accompanied by a written statement by any certified franchising authority with jurisdiction over cable systems affected by the plan of its views concerning the proposed agreement.

Regulatory Flexibility Analysis

Final Regulatory Flexibility Analysis for the Report and Order

Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. Sections 601–12, the Commission's final analysis with respect to the Report and Order is as follows:

Need and purpose of this action: The Commission, in compliance with sections 3 and 14 and those portions of section 9 of the Cable Television Protection and Compliance Act of 1992 (the Act) pertaining to rate regulation, adopts rules and procedures intended to ensure cable subscribers of reasonable rates for cable services with minimum regulatory and administrative burdens on cable entities.

Summary of issues raised by the public comments in response to the Initial Regulatory Flexibility Analysis (IRFA): The Chief Counsel for Advocacy of the United States Small Business Administration ("Office of Advocacy") offers several remarks in response to the IRFA. The Office Advocacy expresses concern that numerous small cable operators cannot operate profitably, if at all, under the constraints imposed by the benchmark. It agrees with the Commission that some other process must be developed to permit small cable operators to demonstrate the reasonableness of rates. The Office of Advocacy believes the Commission's experience with regulation of common carriers may prove beneficial in developing mechanisms that balance the need for exactitude with administrative simplicity.

First, the Office of Advocacy opines that the 1,000 subscriber standard in the 1992 Act does not provide an adequate definition of small operator. It recommends defining small cable operators at those with less than $7.5 million in gross revenues, a standard roughly equivalent to 20–25,000 subscribers. Within this category it recommends separate tiers at 1,000, 3,500, and 10,000 subscribers.

Second, the Office of Advocacy commends the Commission for its compliance with the Regulatory Flexibility Act and its extensive examination of alternative regulatory regimes. It supports the Commission's proposal to streamline cost of service showings for smaller firms, if a relatively simple form can be developed to show what these costs are. It also supports the Commission's proposal of an abbreviated cost showing for significant capital expenditures. The Office of Advocacy also suggests that the Commission consider use of average cost schedules, maintained by an organization of cable operators to provide the same functions for the cable industry that the National Exchange Carrier Association performs for local telephone companies. It opposes use of 1986 rates adjusted for inflation and productivity as an alternative.

Third, the Office of Advocacy also supports considering exemptions for small cable operators, provided certain principles are maintained, including a Commission finding that exempt operators' rates are reasonable.

The Commission also is adopting its proposals for streamlined cost of service studies for small companies, based on a simplified form, and abbreviated cost of service showings for significant capital expenditures. The Commission is also seeking the information needed to consider development of average cost schedules. The Upgrade Incentive Plan that the Commission is adopting on an experimental basis, and seeking comment on, may also be an attractive alternative form of regulation, with substantially reduced administrative burdens, for small operators.

The Commission agrees with the Office of Advocacy that we must ensure that rates for regulated services are reasonable for all cable operators. We are also willing to consider proposals

for pooling cable system costs and revenues in a manner similar to that employed for small telephone companies. It is unclear to us, however, that cable operators are sufficiently interested in such an approach to make its adoption worthwhile. Our consideration of average cost schedule approaches in the Further Notice may provide insight on this matter.

The Commission has also considered the other comments and proposals regarding small cable operators, as we discuss in more detail in the body of the Report and Order. For example, in response to a proposal in comments from Small Systems, we have broadened the definition of small systems for purposes of the cost of service mechanisms to include MSOs with 250,000 or fewer subscribers, who do not own any system with more than 10,000 subscribers, and whose average system size is 1,000 subscribers or less. Interested persons will also have the opportunity to submit further comments on these interim rules in the Further Notice so that we may consider appropriate revisions before these rules become final.

Paperwork Reduction Act

The proposal contained herein has been analyzed with respect to the Paperwork Reduction Act of 1980 and found to impose a new or modified information collection requirement on the public. Implementation of any new or modified requirement will be subject to approval by the Office of Management and Budget as prescribed by the Act.

Ordering Clauses

Accordingly, *It is ordered* That, pursuant to sections 4(i), 4(j), 612, 622(c) and 623 of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), 154(j), 532, 542(c) and 543, the rules, requirements, and policies discussed in the foregoing Report & Order *are adopted*, and that part 76 of the Commission's rules, 47 CFR part 76, *is amended* as set forth below.

It is further ordered that, the rules, policies, and requirements adopted herein *shall be effective* May 15, 1994.

It is further ordered That, the Secretary shall send a copy of this Report and Order, including the certification, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with paragraph 603(a) of the Regulatory Flexibility Act. Public Law 96–354, 94 Stat. 1164, 5 U.S.C. 601 *et seq.* (1981).

It is further ordered That *authority is delegated* to the Chief, Cable Services Bureau to conduct cost studies in conjunction with this proceeding and to develop forms necessary and appropriate to implement this Order.

It is further ordered Pursuant to sections 4(i) 4(j), 623(b), and 623(c) of the Communications Act, 47 U.S.C. 154(i), 154(j), 543 (b) and (c), that the Upgrade Incentive Plan described herein is *adopted on an experimental basis*. Authority is delegated to the Chief, Cable Services Bureau to implement this plan.

List of Subjects in 47 CFR Part 76

Cable television.

Federal Communications Commission.

William F. Caton,

Acting Secretary.

Rule Changes

Part 76 of title 47 of the CFR is amended as follows:

PART 76—CABLE TELEVISION SERVICE

1. The authority citation for part 76 continues to read as follows:

Authority: Secs. 2, 3, 4, 301, 303, 307, 308, 309, 48 Stat., as amended, 1064, 1065, 1066, 1081, 1082, 1083, 1084, 1085, 1101: 47 U.S.C. 152, 153, 154, 301, 303, 307, 308, 309, 532, 533, 535, 542, 543, 552, as amended, 106 Stat. 1460.

2. Section 76.922 is amended by adding paragraphs (g) through (k) to read as follows:

§ 76.922 Rates for the basic service tier and cable programming services tiers.

* * * * *

(g) *Cost of service charge.* (1) For purpose of this section, a monthly cost-of-service charge for a basic service tier or a cable programming service tier is an amount equal to the annual revenue requirement for that their divided by a number that is equal to 12 times the average number of subscribers to that tier during the test year, except that a monthly charge for a system or tier in service less than one year shall be equal to the projected annual revenue requirement for the first 12 months of operation or service divided by a number that is equal to 12 times the projected average number of subscribers during the first 12 months of operation or service. The calculation of the average number of subscribers shall include all subscribers, regardless of whether they receive service at full rates or at discounts.

(2) A test year for an initial regulated charge is the cable operator's fiscal year preceding the initial date of regulation. A test year for a change in the basic service charge that is after the initial date of regulation is the cable operator's fiscal year preceding the mailing or other delivery of written notice pursuant to § 76.932. A test year for a change in a cable programming service charge after the initial rate of regulation is the cable operator's fiscal year preceding the filing of a complaint regarding the increase.

(3) The annual revenue requirement for a tier is the sum of the return component and the expense component for that tier.

(4) The return component for a tier is the average allowable test year ratebase allocable to the tier adjusted for known and measurable changes occurring between the end of the test year and the effective date of the rate multiplied by the rate of return specified by the Commission or franchising authority.

(5) The expense component for a tier is the sum of allowable test year expenses allocable to the tier adjusted for known and measurable changes occurring between the end of the test year and the effective date of the rate.

(6) The ratebase may include the following:

(i) Prudent investment by a cable operator in tangible plant that is used and useful in the provision of cable services less accumulated depreciation. Tangible plant in service shall be valued at the actual money cost (or the money value of any consideration other than money) of property at the time it was first used to provide cable service. The actual money cost of plant may include an allowance for funds used during construction at the prime rate or at the operator's actual cost of funds used during construction. Cost overruns are presumed to be imprudent investment in the absence of a showing that the overrun occurred through no fault of the operator.

(ii) An allowance for start-up losses, if any, that is equal to the lesser of the first two years of operating costs or accumulated losses incurred until the system reached the end of its prematurity stage as defined in Financial Accounting Standards Board Standard 51 ("FASB 51") less straight-line amortization over a reasonable period not exceeding 15 years that commences at the end of the prematurity phase of operation. FASB 51 is available from: Financial Accounting Standards Board, 401 Merritt 7, P.O. Box 5116, Norwalk, CT 06856–5116.

(iii) Intangible assets less amortization that reflect the original costs prudently incurred by a cable operator in organizing and incorporating a company that provides regulated cable services, obtaining a government franchise to provide regulated cable services, or

obtaining patents that are used and useful in the provision of cable services.

(iv) The cost of customer lists if such costs were capitalized during the prematurity phase of operations less amortization.

(v) An amount for working capital to the extent that an allowance or disallowance for funds needed to sustain the ongoing operations of the regulated cable service is demonstrated.

(vi) Other intangible assets to the extent the cable operator demonstrates that the asset reflects costs incurred in an activity or transaction that produced concrete benefits or savings for subscribers to regulated cable services that would not have been realized otherwise and the cable operator demonstrates that a return on such an asset does not exceed the value of such a subscriber benefit.

(vii) The portion of the capacity of plant not currently in service that will be placed in service within twelve months of the end of the test year.

(7) Deferred income taxes shall be deducted from items included in the ratebase.

(8) Allowable expenses may include the following:

(i) All regular expenses normally incurred by a cable operator in the provision of regulated cable service, but not including any lobbying expense, charitable contributions, penalties and fines paid on account of violations of statutes or rules, or membership fees in social, service, recreational or athletic clubs or organizations.

(ii) Reasonable depreciation expense attributable to tangible assets allowable in the ratebase.

(iii) Reasonable amortization expense for prematurely abandoned tangible assets formerly includable in the ratebase that are amortized over the remainder of the original expected life of the asset.

(iv) Reasonable amortization expense for start-up losses and capitalized intangible assets that are includable in ratebase.

(v) Taxes other than income taxes attributable to the provision of regulated cable services.

(vi) An income tax allowance.

(h) *Network upgrade rate increase.* (1) Cable operators that undertake significant network upgrades requiring added capital investment may justify an increase in rates for regulated services by demonstrating that the capital investment will benefit subscribers.

(2) A rate increase on account of upgrades shall not be assessed on customers until the upgrade is complete and providing benefits to customers of regulated services.

(3) Cable operators seeking an upgrade rate increase have the burden of demonstrating the amount of the net increase in costs, taking into account current depreciation expense, likely changes in maintenance and other costs, changes in regulated revenues and expected economies of scale.

(4) Cable operators seeking a rate increase for network upgrades shall allocate net cost increases in conformance with the cost allocation rules as set forth in § 76.924.

(5) Cable operators that undertake significant upgrades shall be permitted to increase rates by adding the benchmark/price cap rate to the rate increment necessary to recover the net increase in cost attributable to the upgrade.

(i) *Hardship rate relief.* A cable operator may adjust charges by an amount specified by the Commission for the cable programming service tier or the franchising authority for the basic service tier if it is determined that:

(1) Total revenues from cable operations, measured at the highest level of the cable operator's cable service organization, will not be sufficient to enable the operator to attract capital or maintain credit necessary to enable the operator to continue to provide cable service;

(2) The cable operator has prudent and efficient management; and

(3) Adjusted charges on account of hardship will not result in total charges for regulated cable services that are excessive in comparison to charges of similarly situated systems.

(j) *Cost of service showing.* A cable operator that elects to establish a charge, or to justify an existing or changed charge for regulated cable service, based on a cost-of-service showing must submit data to the Commission or the franchising authority in accordance with forms established by the Commission. The cable operator must also submit any additional information requested by franchising authorities or the Commission to resolve questions in cost-of-service proceedings.

(k) *Subsequent cost of service charges.* No cable operator may use a cost-of-service showing to justify an increase in any charge established on a cost-of-service basis for a period of 2 years after that rate takes effect, except that the Commission or the franchising authority may waive this prohibition upon a showing of unusual circumstances that would create undue hardship for a cable operator.

3. Section 76.924 is amended by revising paragraphs (b) (c), (d), (e), and (f), redesignating paragraph (g) as paragraph (j), and adding new paragraphs (g) and (i) to read as follows:

§ 76.924 Cost accounting and cost allocation requirements.

* * * * *

(b) *Accounting requirements.* Cable operators electing cost-of-service regulation or seeking rate adjustments due to changes in external costs shall maintain their accounts:

(1) in accordance with generally accepted accounting principles; and

(2) in a manner that will enable identification of appropriate investments, revenues, and expenses.

(c) *Accounts level.* Except to the extent indicated below, cable operators electing cost of service regulation or seeking adjustments due to changes in external costs shall identify investments, expenses and revenues at the franchise, system, regional, and/or company level(s) in a manner consistent with the accounting practices of the operator on April 3, 1993. However, in all events, cable operators shall identify at the franchise level their costs of franchise requirements, franchise fees, local taxes and local programming.

(d) *Summary accounts.* (1) Cable operators filing for cost-of-service regulation, other than small operators, as defined by § 76.922(b)(5)(i), shall report all investments, expenses, and revenue and income adjustments accounted for at the franchise, system, regional and/or company level(s) to the summary accounts listed below:

(i) **Ratebase:**

(A) Net Working Capital.

(B) Headend.

(C) Trunk and Distribution Facilities.

(D) Drops.

(E) Customer Premises Equipment.

(F) Construction/Maintenance Facilities and Equipment.

(G) Programming Production Facilities and Equipment.

(H) Business Offices Facilities and Equipment.

(I) Other Tangible Assets.

(J) Accumulated Depreciation.

(K) Plant Under Construction.

(L) Organizational and Franchise Costs.

(M) Subscriber Lists.

(N) Capitalized Start-up Losses.

(O) Goodwill.

(P) Other Intangibles.

(Q) Accumulated Amortization.

(R) Deferred Taxes.

(ii) **Operating Expenses:**

(A) Cable Plant Employee Payroll.

(B) Cable Plant Power Expense.

(C) Pole Rental, Duct, Other Rental for Cable Plant.

(D) Cable Plant Depreciation Expense.

(E) Cable Plant Expenses—Other.

(F) Plant Support Employee Payroll Expense.
(G) Plant Support Depreciation Expense.
(H) Plant Support Expense—Other.
(I) Programming Activities Employee Payroll.
(J) Programming Acquisition Expense.
(K) Programming Activities Depreciation Expense.
(L) Programming Expense—Other.
(M) Customer Services Expense.
(N) Advertising Activities Expense.
(O) Management Fees.
(P) General and Administrative Expenses.
(Q) Selling General and Administrative Depreciation Expenses.
(R) Selling General and Administrative Expenses—Other.
(S) Amortization Expense—Franchise and Organizational Costs.
(T) Amortization Expense—Customer Lists.
(U) Amortization Expense—Capitalized Start-up Loss.
(V) Amortization Expense—Goodwill.
(W) Amortization Expense—Other Intangibles.
(X) Operating Taxes.
(Y) Other Expenses (Excluding Franchise Fees).
(Z) Franchise Fees.
(AA) Interest on Funded Debt.
(BB) Interest on Capital Leases.
(CC) Other Interest Expenses.
(iii) **Revenue and Income Adjustments:**
(A) Advertising Revenues.
(B) Other Cable Revenue Offsets.
(C) Gains and Losses on Sale of Assets.
(D) Extraordinary Items.
(E) Other Adjustments.

(2) Small operators, as defined by § 76.922(b)(5)(i), that file for cost of service regulation shall report all investments, expenses, and revenue and income adjustments accounted for at the franchise, system, regional and/or company level(s) to the following summary accounts:
(i) **Ratebase:**
(A) Net Working Capital.
(B) Headend, Trunk and Distribution System and Support Facilities and Equipment.
(C) Drops.
(D) Customer Premises Equipment.
(E) Production and Office Facilities, Furniture and Equipment.
(F) Other Tangible Assets.
(G) Accumulated Depreciation.
(H) Plant Under Construction.
(I) Goodwill.
(J) Other Intangibles.
(K) Accumulated Amortization.
(L) Deferred Taxes.
(ii) **Operating Expenses:**
(A) Cable Plant Maintenance, Support and Operations Expense.
(B) Programming Production and Acquisition Expense.
(C) Customer Services Expense.
(D) Advertising Activities Expense.
(E) Management Fees.
(F) Selling, General and Administrative Expenses.
(G) Depreciation Expense.
(H) Amortization Expense—Goodwill.
(I) Amortization Expense—Other Intangibles.
(J) Other Operating Expense (Excluding Franchise Fees).
(K) Franchise Fees.
(L) Interest Expense.
(iii) **Revenue and Income Adjustments:**
(A) Advertising Revenues.
(B) Other Cable Revenue Offsets.
(C) Gains and Losses on Sale of Assets.
(D) Extraordinary Items.
(E) Other Adjustments.

(3) Cable operators shall not be required to report their investments, expenses and revenues to the summary accounts listed in paragraphs (d)(1) and (d)(2) of this section for purposes of adjusting rates based on changes in their external costs.

(e) *Allocation to service cost categories.*

(1) For cable operators electing cost-of-service regulation, investments, expenses, and revenues contained in the summary accounts identified in paragraph (d) of this section shall be allocated among the Equipment Basket, as specified in § 76.923, and the following service cost categories:

(i) Basic service cost category. The basic service category, shall include the cost of providing basic service as defined by § 76.901(a). The basic service cost category may only include allowable costs as defined by §§ 76.922(g) through 76.922(k).

(ii) Cable programming services cost category. The cable programming services category shall include the cost of providing cable programming services as defined by § 76.901(b). This service cost category shall contain subcategories that represent each programming tier that is offered as a part of the operator's cable programming services. All costs that are allocated to the cable programming service cost cateogry shall be further allocated among the programming tiers in this category. The cable programming service cost category may include only allowable costs as defined in § 76.922(g) through 76.922(k).

(iii) Nonregulated cable programming services cost category. The nonregulated cable programming service cost category shall include the cost of providing video programming that is not carried on either the basic service tier or a cable programming service tier. It includes video programming that is offered.
(A) On a pay-per-channel basis;
(B) On a pay-per-program basis; or
(C) As any combination of multiple channels of pay-per-channel or pay-per-program video programming offered on a multiplexed or time-shifted basis so long as the combined service consists of commonly-identified video programming and is not bundled with any regulated tier of service.

(iv) Other cable activities service cost category. The other cable activities service cost category shall include the cost of providing all cable services that are not included in the basic service, cable programming services, or nonregulated cable programming services categories. Other cable activities include leased commercial access, billing and collection services, studio and nonregulated equipment engineering and rental services, sale of nonregulated equipment, and maintenance of nonregulated equipment sold to customers.

(v) Non-cable activities service cost category. The noncable service cost category shall include the cost of providing all activities of a cable operator that are not related to the provision of cable services.

(2) Cable operators seeking an adjustment due to changes in external costs identified in FCC Form 1210 shall allocate such costs among the equipment basket, as specified in § 76.923, and the following service cost categories:

(i) The basic service category as defined by paragraph (e)(1)(i) of this section;

(ii) The cable programming services category as defined by paragraph (e)(1)(ii) of this section;

(iii) The nonregulated cable programming services cost category as defined by paragraph (e)(1)(iii) of this section;

(iv) The other cable activities service costs category as defined by paragraph (e)(1)(iv) of this section; and

(v) The non-cable activities service cost category as defined by paragraph (e)(1)(v) of this section.

(f) *Cost allocation requirements.* (1) Allocations of investments, expenses and revenues among the service cost categories and the equipment basket shall be made at the organizational level in which such costs and revenues have been identified for accounting purposes pursuant to § 76.924(c).

(2) Costs of programming and retransmission consent fees shall be

directly assigned or allocated only to the service cost category in which the programming or broadcast signal at issue is offered.

(3) Costs of franchise fees shall be allocated among the equipment basket and the service cost categories in a manner that is most consistent with the methodology of assessment of franchise fees by local authorities.

(4) Costs of public, educational, and governmental access channels carried on the basic tier shall be directly assigned to the basic tier where possible.

(5) All other costs that are incurred exclusively to support the equipment basket or a specific service cost category shall be directly assigned to that service cost category or the equipment basket where possible.

(6) Costs that are not directly assigned shall be allocated to the service cost categories in accordance with the following allocation procedures:

(i) Wherever possible, common costs for which no allocator has been specified by the Commission are to be allocated among the service cost categories and the equipment basket based on direct analysis of the origin of the costs.

(ii) Where allocation based on direct analysis is not possible, common costs for which no allocator has been specified by the Commission shall, if possible, be allocated among the service costs categories and the equipment basket based on indirect, cost-causative linkage to other costs directly assigned or allocated to the service cost categories and the equipment basket.

(iii) Where neither direct nor indirect measures of cost allocation can be found, common costs shall be allocated to each service cost category based on the ratio of all other costs directly assigned and attributed to a service cost category over total costs directly or indirectly assigned and directly or indirectly attributable.

(g) *Cost identification at the franchise level.* After costs have been directly assigned to and allocated among the service cost categories and the equipment basket, cable operators that have aggregated costs at a higher level than the franchise level must identify all applicable costs at the franchise level in the following manner:

(1) Recoverable costs that have been identified at the highest organizational level at which costs have been identified shall be allocated to the next (lower) organizational level at which recoverable costs have been identified on the basis of the ratio of the total number of subscribers served at the lower level to the total number of subscribers served at the higher level.

(2) Cable operators shall repeat the procedure specified in paragraph (g)(1) of this section at every organizational level at which recoverable costs have been identified until such costs have been allocated to the franchise level.

* * * * *

(i) *Transactions and affiliates.* Adjustments on account of external costs and rates set on a cost-of-service basis shall exclude any amounts not calculated in accordance with the following:

(1) Charges for assets purchased by or transferred to the regulated activity of a cable operator from affiliates shall equal the invoice price if that price is determined by a prevailing company price. The invoice price is the prevailing company price if the affiliate has sold a substantial number of like assets to nonaffiliates. If a prevailing company price for the assets received by the regulated activity is not available, the changes for such assets shall be the lower of their cost to the originating activity of the affiliated group less all applicable valuation reserves, or their fair market value.

(2) The proceeds from assets sold or transferred from the regulated activity of the cable operator to affiliates shall equal the prevailing company price if the cable operator has sold a substantial number of like assets to nonaffiliates. If a prevailing company price is not available, the proceeds from such sales shall be determined at the higher of cost less all applicable valuation reserves, or estimated fair market value of the asset.

(3) Charges for services provided to the regulated activity of a cable operator by an affiliate shall equal the invoice price if that price is determined by a prevailing company price. The invoice price is the prevailing company price if the affiliate has sold like services to a substantial number of nonaffiliates. If a prevailing company price for the services received by the regulated activity is not available, the charges of such services shall be at cost.

(4) The proceeds from services sold or transferred from the regulated activity of the cable operator to affiliates shall equal the prevailing company price if the cable operator has sold like services to a substantial number of nonaffiliates. If a prevailing company price is not available, the proceeds from such sales shall be determined at cost.

(5) For purposes of § 76.924(i)(1) through 76.924(i)(4), costs shall be determined in accordance with the standards and procedures specified in § 76.922 and paragraphs (b) and (d) of this section.

[FR Doc. 94–9078 Filed 4–14–94; 8:45 am]
BILLING CODE 6712–01–M

DEPARTMENT OF TRANSPORTATION

National Highway Traffic Safety Administration

49 CFR Part 571

[Docket No. 74–14; Notice 87]

RIN 2127–AE79

Federal Motor Vehicle Safety Standards; Occupant Crash Protection; Seat Belt Assemblies

AGENCY: National Highway Traffic Safety Administration (NHTSA), DOT.

ACTION: Final rule.

SUMMARY: This final rule allows manufacturers of all replacement seat belt assemblies intended for use only in specifically stated motor vehicles a choice of two means of providing information regarding the seating positions and vehicle models for which the assemblies are appropriate. The information may be provided either on the assembly itself or in the installation instruction sheet currently required to accompany the assembly. This final rule also removes the labeling requirement for two types of seat belt assemblies when they are installed as original equipment in a new motor vehicle. NHTSA believes that this final rule provides manufacturers more flexibility in the manner of providing this information without decreasing the likelihood that belts will be correctly installed.

DATES: *Effective Date:* The amendments made in this rule are effective October 12, 1994.

Petition Date: Any petitions for reconsideration must be received by NHTSA no later than May 16, 1994.

ADDRESSES: Any petitions for reconsideration should refer to the docket and notice number of this notice and be submitted to: Administrator, National Highway Traffic Safety Administration, 400 Seventh Street, SW., Washington, DC 20590.

FOR FURTHER INFORMATION CONTACT: Mr. Daniel S. Cohen, Office of Vehicle Safety Standards, NRM–12, National Highway Traffic Safety Administration, 400 Seventh Street, SW., Washington, DC 20590. Telephone: (202) 366–4911.

SUPPLEMENTARY INFORMATION:

Background

Standard No. 209 takes three different approaches to requiring manufacturers of replacement seat belt assemblies to provide information regarding the vehicle models and seating positions for which the assemblies are appropriate. The standard requires some seat belt assemblies to be labeled, some to be both labeled and accompanied by an installation instruction sheet, and some to be accompanied by an installation instruction sheet. The following belts are required to be labeled:

- Dynamically tested belts with load limiters installed in new motor vehicles (section S4.5(c)); and
- Dynamically tested manual belts installed in new trucks and multipurpose passenger vehicles with a gross vehicle weight rating of 8,500 pounds or less and an unloaded weight of less than 5,500 pounds (LTVs) (section S4.6(b)).

The following belts are required to be both labeled and accompanied by an installation instruction sheet:

- Dynamically tested replacement belts with load limiters (sections S4.1(k) and S4.5(c)); and
- Dynamically tested manual replacement belts for LTVs (sections S4.1(k) and S4.6(b)).

All other replacement belts are required to be accompanied by an installation instruction sheet (section S4.1(k)).

On May 10, 1993, NHTSA published a notice of proposed rulemaking (NPRM) proposing to replace these three different sets of requirements with a single provision allowing manufacturers of replacement seat belt assemblies a choice of one of two means of providing information regarding the seating positions and vehicle models for which the assemblies are appropriate: Either on the assembly or in the installation instruction sheet currently required to accompany the assembly. The NPRM also proposed to exclude from the proposed labeling requirement those seat belt assemblies that are installed as original equipment in a new motor vehicle.

NHTSA received six comments on the NPRM. Four of the commenters supported the agency's adopting the amendments proposed in the NPRM. None of the commenters objected to the proposed exclusion of seat belt assemblies installed as original equipment. This exclusion has been adopted as proposed.

General Motors (GM) raised issues regarding the types of replacement belts subject to the two proposed options, regarding the means of providing the required information, and regarding the effect of the proposal on current inventories. Volkswagen (VW) suggested that the agency rescind the requirement to provide installation instructions. All of the comments were considered in the formulation of this final rule and are addressed below. Since the final rule will provide manufacturers more flexibility in the manner of providing installation information without decreasing the likelihood that belts will be correctly installed, NHTSA is adopting the provision regarding the choice of two means of providing the information as proposed.

Note: On May 28, 1993, the Association of International Automobile Manufacturers submitted a petition for rulemaking requesting the agency to rescind the requirement that replacement seat belt assemblies be accompanied by installation instructions. Elsewhere in this issue of the Federal Register, the agency has published a notice denying this petition.

Applicability

In the NPRM, NHTSA proposed a 30 day leadtime based on its belief that all belts which comply with the current requirements would comply with the new requirement. GM disagreed with this assumption. GM correctly stated that make/model information is currently required only on certain dynamically tested belts. The proposed language required this information to be either on all replacement belts or on the instruction sheet for all replacement belts.

This final rule will require the addition of only one sentence on either the belt or the instruction sheet for some dynamically tested belts. For all other replacement belts, no change will be necessary. In order to provide manufacturers with sufficient time to design, fabricate, and attach new labels, or to change, edit, and approve the additional text for the instruction sheet to be provided with the replacement belt assembly, NHTSA has provided for a leadtime of 180 days.

Current Inventories

GM also expressed concern that the proposed requirement would apply to replacement belts in inventory which had not been installed prior to the effective date of the final rule. GM is incorrect. Only products manufactured on or after the effective date of an applicable requirement in a Federal motor vehicle safety standard must comply with that requirement. Therefore, only replacement belt assemblies manufactured on or after the effective date of the final rule would be required to comply with the new requirements.

Allow "Alternative Means" or Rescind Requirement

Citing recent agency grants of petitions for inconsequential noncompliance with S4.1(k) of Standard No. 209, GM suggested that the agency should amend the proposed language to allow other "alternative means" of providing installation information in addition to placing it on the belt or on an instruction sheet in the box. GM did not identify any specific "alternative means" or provide any other guidance on how the agency would determine that a seat belt assembly met such a requirement. Also citing the grants of petitions for inconsequential noncompliance, VW suggested that the agency should rescind the requirement to provide installation instructions completely. As explained below, the agency disagrees with both commenters.

With regard to GM's request that "alternative means" of providing the required information be allowed, NHTSA believes that the language suggested by GM is not sufficiently objective to satisfy the requirements of the National Traffic and Motor Vehicle Safety Act (15 U.S.C. 1381 *et seq.*). Therefore, NHTSA has not altered the proposed language as GM suggested.

With regard to VW's comment, the agency notes that since November 5, 1992, it has received seven petitions for inconsequential noncompliance because replacement belt assemblies were not accompanied by required installation information. These petitions were granted because the petitioner demonstrated that the noncompliance was inconsequential due to other procedures or practices that provided the information in another format than that required by Standard No. 209. The other procedures or practices involved a determination by a mechanic or technician of physical differences unique to a particular design. These practices and procedures may work well, but their success depends on the vigilance and experience of the installer. VW did not provide any information indicating that any of these procedures or practices would ensure that an untrained person could correctly install the belts. NHTSA notes that not all belts are replaced by a trained mechanic. Moreover, a change in the standard to remove this requirement would substantially magnify the potential risk of improper installation, given that no evidence was provided that all seat belt or vehicle manufacturers have such a practice or procedure.

The grant of a petition for inconsequential noncompliance exempts the manufacturer from the notification and remedy requirements of the National Traffic and Motor Vehicle Safety Act (15 U.S.C. 1381 *et seq.*). An inconsequentiality proceeding is retrospective, and, in the case of the failure to provide installation instructions, the granting of petitions was based, in part, on the fact that there was no evidence that any of the replacement belt assemblies had been installed incorrectly. A rulemaking proceeding is, by contrast, prospective, looking at whether all future seat belt assemblies should be excluded from the requirement to provide installation information. VW did not demonstrate that the installation information would get to all users in a reliable and effective manner absent the requirement that it be provided with the belt. Thus, NHTSA disagrees with VW that this requirement should be rescinded.

Rulemaking Analyses and Notices

Executive Order 12866 and DOT Regulatory Policies and Procedures

NHTSA has considered the impact of this rulemaking action under Executive Order 12866 and the Department of Transportation's regulatory policies and procedures. This action was not reviewed under the Executive Order. With respect to the DOT policies and procedures, this action has been determined not to be significant. This final rule allows manufacturers an option of either providing information with seat belt assemblies or labeling the seat belt assemblies. Except for some dynamically tested belts, seat belt assemblies currently are required to comply with one of these options. The cost savings associated with deleting some of the requirements should more than offset any additional minor costs associated with adding make/model information to the installation instruction sheets. Therefore, the agency has determined that there will be minimal additional costs with respect to some assemblies.

Regulatory Flexibility Act

NHTSA has also considered the impacts of this final rule under the Regulatory Flexibility Act. I hereby certify that this rule will not have a significant economic impact on a substantial number of small entities. As explained above, the agency has determined that this final rule will have only a minimal cost impact on some seat belt assemblies. Accordingly, a regulatory evaluation has not been prepared for this final rule.

Paperwork Reduction Act

In accordance with the Paperwork Reduction Act of 1980 (Pub. L. 96–511), there are no requirements for information collection associated with this final rule.

National Environmental Policy Act

NHTSA has also analyzed this final rule under the National Environmental Policy Act and determined that it will not have a significant impact on the human environment.

Executive Order 12612 (Federalism)

Finally, NHTSA has analyzed this rule in accordance with the principles and criteria contained in Executive Order 12612, and has determined that this rule will not have significant federalism implications to warrant the preparation of a Federalism Assessment.

Civil Justice Reform

This final rule does not have any retroactive effect. Under section 103(d) of the National Traffic and Motor Vehicle Safety Act (Safety Act; 15 U.S.C. 1392(d)), whenever a Federal motor vehicle safety standard is in effect, a State may not adopt or maintain a safety standard applicable to the same aspect of performance which is not identical to the Federal standard, except to the extent that the State requirement imposes a higher level of performance and applies only to vehicles procured for the State's use. Section 105 of the Safety Act (15 U.S.C. 1394) sets forth a procedure for judicial review of final rules establishing, amending or revoking Federal motor vehicle safety standards. That section does not require submission of a petition for reconsideration or other administrative proceedings before parties may file suit in court.

List of Subjects in 49 CFR Part 571

Imports, Motor vehicle safety, Motor vehicles.

PART 571—FEDERAL MOTOR VEHICLE SAFETY STANDARDS

In consideration of the foregoing, 49 CFR part 571 is amended as follows:

1. The authority citation for part 571 of title 49 continues to read as follows:

Authority: 15 U.S.C. 1392, 1401, 1403, 1407, delegation of authority at 49 CFR 1.50.

§ 571.208 [Amended]

2. Section 571.208 is amended by adding a new S4.5.3.5 to read as follows:

§ 571.208 Standard No. 208; Occupant crash protection.

* * * * *

S4.5.3.5 A replacement automatic belt shall meet the requirements of S4.1(k) of Standard No. 209.

* * * * *

§ 571.209 [Amended]

3. Section 571.209 is amended by removing S4.5(c) and S4.6(b), and by revising S4.1(k) to read as follows:

§ 571.209 Standard No. 209; Seat belt assemblies.

* * * * *

S4.1 * * *

* * * * *

(k) *Installation instructions.* A seat belt assembly, other than a seat belt assembly installed in a motor vehicle by an automobile manufacturer, shall be accompanied by an instruction sheet providing sufficient information for installing the assembly in a motor vehicle. The installation instructions shall state whether the assembly is for universal installation or for installation only in specifically stated motor vehicles, and shall include at least those items specified in SAE Recommended Practice J800c, "Motor Vehicle Seat Belt Installations," November 1973. If the assembly is for use only in specifically stated motor vehicles, the assembly shall either be permanently and legibly marked or labeled with the following statement, or the instruction sheet shall include the following statement:

This seat belt assembly is for use only in [insert specific seating position(s), e.g., "front right"] in [insert specific vehicle make(s) and model(s)].

* * * * *

Issued on April 11, 1994.

Christopher A. Hart,

Deputy Administrator.

[FR Doc. 94–9086 Filed 4–14–94; 8:45 am]

BILLING CODE 4910–59–P

DEPARTMENT OF THE INTERIOR

Fish and Wildlife Service

50 CFR Part 17

RIN 1018–AC01

Endangered and Threatened Wildlife and Plants; Determination of Endangered Status for the Royal Snail and Anthony's Riversnail

AGENCY: Fish and Wildlife Service, Interior.

ACTION: Final rule.

SUMMARY: The U.S. Fish and Wildlife Service (Service) determines endangered status for the royal snail (*Pyrgulopsis* (=*Marstonia*) *ogmorhaphe*) and Anthony's riversnail (*Athearnia*

anthonyi) under the Endangered Species Act of 1973, as amended (Act). The royal snail is known only from two spring runs on public lands in the Sequatchie River system, Marion County, Tennessee. The extremely limited distribution of the royal snail and the limited amount of occupied habitat make this species extremely vulnerable to extinction. Anthony's riversnail is known from two small populations—one in the Sequatchie River, Marion County, Tennessee, and one in Limestone Creek, Limestone County, Alabama. These populations are threatened by the general water quality deterioration that has resulted from siltation and other pollutants contributed by such factors as coal mining, poor land use practices, and waste discharges. The protection and recovery provisions afforded by the Act for the royal snail and Anthony's riversnail are implemented by this final rule.

EFFECTIVE DATE: May 16, 1994.

ADDRESSES: The complete file for this rule is available for public inspection, by appointment, during normal business hours at the Asheville Field Office, U.S. Fish and Wildlife Service, 330 Ridgefield Court, Asheville, North Carolina 28806.

FOR FURTHER INFORMATION CONTACT: Mr. J. Allen Ratzlaff or Mr. Richard G. Biggins at the above address (704/665–1195, Ext. 229 or 228, respectively).

SUPPLEMENTARY INFORMATION:

Background

Royal Snail

The royal snail (*Marstonia ogmorhaphe*) was described by Thompson in 1977 and was later reassigned to the genus *Pyrgulopsis* by Hershler and Thompson (1987). The royal snail is a small (usually less than 5 millimeters (0.25 inch) in length) annual species distinguished from other closely related species by (1) its relatively large size; (2) its large number of whorls (5.2 to 5.8); (3) its deeply incised, suture-producing, strongly shouldered whorls, which are almost flat above; (4) its complete aperture, which is broadly ovate in shape with a rounded posterior corner; (5) its outer lip, which is slightly arched forward in lateral profile; (6) its thin shell; (7) its conical-terete shape; and (8) its enlarged bursa copulatrix with a completely exposed duct (Thompson 1977).

The royal snail is known from only two spring runs in the Sequatchie River system in Marion County, Tennessee. Royal snails are generally found in the diatomaceous "ooze" and on leaves and twigs in the quieter pools downstream from the spring source.

While no populations of the royal snail are known to have been lost, the general deterioration of the water quality that has resulted from siltation and other pollutants contributed by coal mining, poor land use practices, and waste discharges likely are impacting the species. This could result in serious, irreversible decline of the species. Additionally, because both existing populations inhabit extremely limited areas, they are very vulnerable to extirpation from accidental toxic chemical spills or vandalism.

On December 17, 1992, the Service notified by mail (28 letters) the potentially affected Federal and State agencies, local governments, and interested individuals within the species' present range that a status review of the royal snail was being conducted. Three agencies and one private organization responded. The Tennessee Valley Authority supported proposing the species for listing. The Tennessee Wildlife Resources Agency, U.S. Soil Conservation Service, and the one responding private organization did not take a position on the potential listing. No objections to the potential listing of the royal snail were received.

Anthony's Riversnail

Anthony's riversnail was originally described from specimens collected in the Holston River, near Knoxville, Tennessee ("Budd," in Redfield 1854). This relatively large freshwater snail, which grows to about 2.5 centimeters (1 inch) in length, is ovate and olive green to yellowish brown in color. Anthony's riversnail is listed by the Tennessee Department of Environment and Conservation as a threatened species (Bogan and Parmalee 1983).

Anthony's riversnail is primarily a big-river species that was historically associated with shoal areas in the main stem of the Tennessee River and the lower reaches of some of its tributaries. There are historical records of the species from the lower French Broad River, Knox County, Tennessee; Nolichucky River, Green County, Tennessee; Clinch River, Jefferson County, Tennessee; Beaver Creek, Knox County, Tennessee; Little Tennessee River, Monroe and Loudon Counties, Tennessee; Tellico River, Monroe County, Tennessee; Sequatchie and Little Sequatchie Rivers and Battle Creek, Marion County, Tennessee; South Chickamauga and Tiger Creeks, Catoosa County, Georgia; Limestone Creek, Limestone County, Alabama; and Tennessee River, Knox and Loudon Counties, Tennessee, and Jackson, Limestone, and Lauderdale Counties, Alabama (Bogan and Parmalee 1983; Gordon 1991; F. Thompson, Florida Museum of Natural History, personal communication, 1991). Presently, only two small populations are known to survive—one in the Sequatchie River, Marion County, Tennessee (M. Gordon, Tennessee Technological University, and S. Ahlstedt, Tennessee Valley Authority, personal communications 1991), and one in Limestone Creek, Limestone County, Alabama (Thompson, personal communication, 1991; Garner 1992). Many populations were lost when much of the Tennessee River and the lower reaches of its tributaries were impounded. The general water quality deterioration that has resulted from siltation and other pollutants contributed by coal mining, poor land use practices, and waste discharges was likely responsible for the species' further decline. These factors continue to impact the Sequatchie River and Limestone Creek populations.

Both existing populations inhabit short river reaches; thus, they are very vulnerable to extirpation from accidental toxic chemical spills. As the Sequatchie River and Limestone Creek are isolated by impoundments from other Tennessee River tributaries, recolonization of any extirpated populations would be unlikely without human intervention. Additionally, because these populations are isolated, their long-term genetic viability is questionable.

Anthony's riversnail (*Athearnia anthonyi*) first appeared as a candidate species (category 2) on May 22, 1984, in the Invertebrate Notice or Review (49 FR 21664–21675). This taxon was reassigned from category 2 to category 3B on January 6, 1989, in the Animal Notice of Review (54 FR 554–579). The change in category was based on information that Anthony's riversnail was not a distinct species, but that it was instead the same as another category 2 species, the boulder snail (*Leptoxis* (=*Athearnia*) *crassa*). Gordon (1991) examined juveniles of both species and concluded that the two snails are distinct species. However, as the boulder snail is apparently extinct (Bogan and Parmalee 1983, Gordon 1991), their distinctiveness is irrelevant.

On June 12, 1992, the Service notified by mail (37 letters) the potentially affected Federal and State agencies, local governments, and interested individuals within the species' present range that a status review of the Anthony's riversnail was being conducted. Four agencies responded. The Tennessee Department of Environment and Conservation

supported proposing the species for listing. The Tennessee Valley Authority, U.S. Soil Conservation Service, and Tennessee State Planning Office responded to the notification letter but did not take a position on the potential listing. No objections to the potential listing of the Anthony's riversnail were received.

Summary of Comments and Recommendations

In the August 5, 1993, proposed rule (58 FR 41690) on the royal snail and Anthony's riversnail and through associated notifications, all interested parties were requested to submit factual reports and information that might contribute to the development of a final rule for the royal snail and Anthony's riversnail. Appropriate Federal and State agencies, and interested parties were contacted by letters dated August 16, 1993. Legal notices were published in the Chattanooga Times and Chattanooga News-Free Press on August 19, 1993, and in the Decatur Daily on August 23, 1993.

One written comment was received on the proposed rule to list the royal snail an Anthony's riversnail. The U.S. Soil Conservation Service responded by stating they had no additional information on either of the species.

Summary of Factors Affecting the Species

After a thorough review and consideration of all information available, the Service has determined that the royal snail and Anthony's riversnail should be classified as endangered species. Section 4(a)(1) of the Act and regulations (50 CFR part 424) promulgated to implement the listing provisions of the Act were followed. A species may be determined to be an endangered or threatened species due to one or more of the five factors described in section 4(a)(1). These factors and their application to the royal snail (*Pyrgulopsis* (=*Marstonia*) *ogmorhaphe*) and Anthony's riversnail (*Athearnia anthonyi*) are as follows:

A. The Present or Threatened Destruction, Modification, or Curtailment of Its Habitat or Range

The royal snail is known from only two spring runs in the Sequatchie River system in Marion County, Tennessee, and has never been found outside these areas. This extremely limited distribution, the limited amount of occupied habitat, the ease of accessibility, and the species' annual life cycle make the royal snail extremely vulnerable to extinction. Threats to the species include siltation; road construction; logging; agricultural, municipal, industrial, and mining runoff (both direct and from sub surface flows); cattle grazing; vandalism; and pollution from trash thrown in the springs. Further, timber harvesting for wood chip mills proposed for southeastern Tennessee and northeastern Alabama could impact this species.

Anthony's riversnail was once rather widespread in the Tennessee River system. (See "Background" section for a discussion of the species' historic range.) Presently, only two small populations are known to survive—one in the Sequatchie River, Marion County, Tennessee (Gordon and Ahlstedt, personal Communications, 1991), and one in Limestone Creek, Limestone County, Alabama (Thompson, personal Communication, 1991; Garner 1992).

Anthony's riversnail is primarily a big-river species that was historically associated with shoal areas in the main stem of the Tennessee River and the lower reaches of some of its tributaries. When the Tennessee River impoundments were constructed, most of the Tennessee River's riverine habitat was lost, and the lower reaches of its tributaries were also inundated. Populations that were able to survive in the remaining limited unimpounded habitat were apparently lost due to the general deterioration of water quality that has resulted from siltation and other pollutants contributed by coal mining, poor land use practices, and waste discharges. These factors continue to impact the Sequatchie River and Limestone Creek populations. Additionally, timber harvesting for wood chip mills proposed for southeastern Tennessee and northeastern Alabama could impact the species.

B. Overutilization for Commercial, Recreational, Scientific, or Educational Purposes

There is no indication that over-utilization has been a problem for the royal snail or Anthony's riversnail. The specific areas inhabited by these species are presently not known by the general public; until the proposed rule was published, they were likely unaware of the presence of these rare snails. If the specific areas inhabited by these two species were revealed, it would be extremely easy for vandals to seriously impact them. Therefore, the present range of these species has been described only in general terms.

C. Disease or Predation

Although the royal snail and Anthony's riversnail are consumed by predatory animals, there is no evidence that predation or disease are serious threats to the species.

D. The Inadequacy of Existing Regulatory Mechanisms

The State of Tennessee prohibits taking fish and wildlife, including freshwater snails, for scientific purposes without a State collecting permit. However, the royal snail and Anthony's riversnail are generally not protected from other threats. Federal listing will provide additional protection for these species from collectors by requiring Federal endangered species permits to take these species and by requiring Federal agencies to consult with the Service when projects they fund, authorize, or carry out may affect the species.

E. Other Natural or Manmade Factors Affecting its Continued Existence

Because the royal snail is presently restricted to two small spring runs, it is very vulnerable to extinction from accidental toxic chemical spills; and because the populations are physically isolated from each other, recolonization of an extirpated population would not be possible without human intervention. Additionally, because natural gene flow among populations is not possible, the long-term genetic viability of these remaining isolated populations is questionable.

Both existing Anthony's riversnail populations inhabit short river reaches; thus, they are vulnerable to extirpation from accidental toxic chemical spills. As the Sequatchie River and Limestone Creek are isolated by impoundments from other Tennessee River tributaries, recolonization of any extirpated populations would be unlikely without human intervention. Additionally, because these populations are isolated, their long-term genetic viability is questionable.

The Service has carefully assessed the best scientific and commercial information available regarding the past, present, and future threats faced by these species in determining to make this rule final. Based on this evaluation, the preferred action is to list the royal snail and Anthony's riversnail as endangered. The royal snail is known from only two populations in spring runs in Marion County, Tennessee. Anthony's riversnail is currently known from two small populations—one in the Sequatchie River, Marion County, Tennessee, and one in Limestone Creek, Limestone County, Alabama. These snails and their habitats have been and continue to be threatened, and Anthony's riversnail has undergone a

significant range reduction. Their limited distribution also makes them vulnerable to toxic chemical spills. Because of their restricted distributions and both snails' vulnerability to extinction, endangered status appear to be the most appropriate classification for these species. (See "Critical Habitat" for a discussion of why critical habitat is not being designated for these snails.)

Critical Habitat

Section 4(a)(3) of the Act, as amended, requires that, to the maximum extent prudent and determinable, the Secretary designate critical habitat at the time the species is determined to be endangered or threatened. The Service's regulations (50 CFR 424.12(a)(1)) state that designation of critical habitat is not prudent when one or both of the following situations exist:

(1) The species is threatened by taking or other activity and the identification of critical habitat can be expected to increase the degree of threat to the species or

(2) The designation of critical habitat would not be beneficial to the species. The Service finds that designation of critical habitat is not presently prudent for these species. Such a determination would result in no known benefit to these species, and designation of critical habitat could further threaten both species.

Section 7(a)(2) and regulations codified at 50 CFR part 402 require Federal agencies to ensure, in consultation with and with the assistance of the Service, that activities they authorize, fund, or carry out are not likely to jeopardize the continued existence of listed species or destroy or adversely modify its critical habitat, if designated. Section 7(a)(4) requires Federal agencies to confer informally with the Service on any action that is likely to jeopardize the continued existence of a proposed species or result in the destruction or adverse modification of proposed critical habitat. (See "Available Conservation Measures" section for a further discussion of section 7.) As part of the development of the proposed rules, Federal and State agencies were notified of the snail's general distribution, and they were requested to provide data on proposed Federal actions that might adversely affect the two species. No specific projects were identified. Should any future projects be proposed in areas inhabited by these snails, the involved Federal agency will already have the general distributional data needed to determine if the species may be impacted by their action; if needed, more specific distributional information would be provided.

Each of these snails occupies very restricted stream reaches. Thus, as any significant adverse modification or destruction of these species' habitat would likely jeopardize their continued existence, no additional protection for the species would accrue from critical habitat designation that would not also accrue from listing the species. Therefore, habitat protection for these species will be accomplished through the section 7 jeopardy standard and section 9 prohibitions against take.

In addition, because these species are very rare, with populations restricted to extremely short stream reaches, unregulated taking for any purpose could threaten their continued existence. The publication of critical habitat maps in the **Federal Register** and local newspapers and any other publicity accompanying critical habitat designation could increase the collection threat and increase the potential for vandalism, especially during the often controversial critical habitat designation process. (See "Summary of Factors Affecting the Species" section for a further discussion of threats to these species from vandals.) The locations of populations of these species have consequently been described only in general terms in this final rule. Precise locality data is available to appropriate Federal, State, and local government agencies and individuals from the service office described in the **ADDRESSES** section and from the Service's Cookeville Field Office, 446 Neal Street, Cookeville, Tennessee 38501.

Available Conservation Measures

Conservation measures provided to species listed as endangered or threatened under the Endangered Species Act include recognition, recovery actions, requirements for Federal protection, and prohibitions against certain practices. Recognition through listing encourages and results in conservation actions by Federal, State, local, and private agencies, groups, and individuals. The Act provides for possible land acquisition and cooperation with the States and requires that recovery actions be carried out for all listed species. The protection required of Federal agencies and the prohibitions against taking and harm are discussed, in part, below.

Section 7(a) of the Act, as amended, requires Federal agencies to evaluate their actions with respect to any species that is proposed or listed as endangered or threatened and with respect to its critical habitat, if any is being designated. Regulations implementing this interagency cooperation provision of the Act are codified at 50 CFR part 402. Section 7(a)(2) requires Federal agencies to ensure that activities they authorize, fund, or carry out are not likely to jeopardize the continued existence of a listed species or to destroy or adversely modify its critical habitat. If a Federal action may affect a listed species or its critical habitat, the responsible Federal agency must enter into formal consultation with the Service.

The Service notified Federal agencies that could have programs affecting these species. No specific proposed Federal actions were identified that would likely affect the species. Federal activities that could occur and impact the species include, but are not limited to, the carrying out or the issuance of permits for reservoir construction, stream alterations, wastewater facility development, pesticide registration, and road and bridge construction. It has been the experience of the Service, however, that nearly all Section 7 consultations can be resolved so that the species is protected and the project objectives are met.

The Act and implementing regulations found at 50 CFR 17.21 set forth a series of general prohibitions and exceptions that apply to all endangered wildlife. These prohibitions, in part, make it illegal for any person subject to the jurisdiction of the United States to take (include harass, harm, pursue, hunt, shoot, wound, kill, trap, or collect; or to attempt any of these), import or export, ship in interstate commerce in the course of commercial activity, or sell or offer for sale in interstate or foreign commerce any listed species. It also is illegal to possess, sell, deliver, carry, transport, or ship any such wildlife that has been taken illegally. Certain exceptions apply to agents of the Service and State conservation agencies.

Permits may be issued to carry out otherwise prohibited activities involving endangered wildlife species under certain circumstances. Regulations governing permits are at 50 CFR 17.22 and 17.23. Such permits are available for scientific purposes, to enhance the propagation or survival of the species, and/or for incidental take in connection with otherwise lawful activities. In some instances, permits may be issued for a specified time to relieve undue economic hardship that would be suffered if such relief were not available. These species are not in trade, and such permit requests are not expected.

National Environmental Policy Act

The Fish and Wildlife Service has determined that an Environmental Assessment, as defined under the authority of the National Environmental Policy Act of 1969, need not be prepared in connection with regulations adopted pursuant to section 4(a) of the Endangered Species Act of 1973, as amended. A notice outlining the Service's reasons for this determination was published in the **Federal Register** on October 25, 1983 (48 FR 49244).

References Cited

Bogan, A. E., and P. W. Parmalee. 1983. Tennessee's rare wildlife, Volume II: the mollusks. 123 pp.

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Author

The primary authors of this final rule are Mr. J. Allen Ratzlaff and Mr. Richard G. Biggins (see **ADDRESSES** section) (704/665–1195, Ext. 229 and 228, respectively).

List of Subjects in 50 CFR Part 17

Endangered and threatened species, Exports, Imports, Reporting and recordkeeping requirements, and Transportation.

Regulation Promulgation

Accordingly, part 17, subchapter B of chapter I, title 50 of the Code of Federal Regulations, is amended as set forth below:

PART 17—[AMENDED]

1. The authority citation for part 17 continues to read as follows:

Authority: 16 U.S.C. 1361–1407; 16 U.S.C. 1531–1544; 16 U.S.C. 4201–4245; Pub. L. 99–625, 100 Stat. 3500; unless otherwise noted.

2. Amend § 17.11(h) by adding the following, in alphabetical order, under snails, to the List of Endangered and Threatened Wildlife, to read as follows:

§ 17.11 Endangered and threatened wildlife.

* * * * *

(h) * * *

Species		Historic range	Vertebrate population where endangered or threatened	Status	When listed	Critical habitat	Special rules
Common name	Scientific name						
SNAILS							
*	*	*	*	*	*	*	*
Snail, royal	*Pyrgulopsis* (=*Marstonia*) *oqmorhaphe.*	U.S.A. (TN)	NA	E	438	NA	NA
*	*	*	*	*	*	*	*
Riversnail, Anthony's	*Athearnia anthonyi*	U.S.A. (AL, GA, TN)	NA	E	438	NA	NA
*	*	*	*	*	*	*	*

Dated: April 1, 1994.

Mollie H. Beattie,

Director, Fish and Wildlife Service.

[FR Doc. 94–9070 Filed 4–14–94; 8:45 am]

BILLING CODE 4310–55–M